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Politics this week

Aug 15th 2002
From The Economist print edition

After Saddam

Saddam Hussein is still in office, but it was disclosed this week that America's State Department is already inviting bids from organisations that could provide **humanitarian relief in Iraq** after he is ousted.

President George Bush took a break from his holiday to meet "**ordinary Americans**" at a carefully planned forum to discuss the economy in Waco, Texas. He promised to prevent Congress spending an extra $5.1 billion in an amendment to an anti-terrorism bill.

AP

See article: George Bush's economic summit

Oregon's biggest blaze for a century was fought back by more than 6,000 firefighters. So far this year, wildfires in America have burned 5.5m acres.

See article: Fighting fires, losing the war

A biological-weapons researcher in Maryland denied having anything to do with the letters containing **anthrax** that killed five people last year. Steven Hatfill lost his job after his flat was searched by the FBI, which has yet to arrest anyone for sending the anthrax-laden letters.

Officials overseeing the redevelopment of the site of the **World Trade Centre** opened up the search for new designs, belatedly admitting that their bland first proposals "lacked spunk".

Pakistan's bad image

Pakistan's president, Pervez Musharraf, underlined his support for the "principled" struggle of separatists in Indian-ruled Kashmir while condemning Islamic extremists for tarnishing Pakistan's image. India accused him of double standards.

A **Sri Lankan** minister met the Tamil Tigers' chief negotiator in Norway's capital, Oslo, to agree an agenda for much-delayed peace talks. A Norwegian-backed ceasefire agreement was adopted in February. The talks are due to start next month.

An Indonesian court sentenced **East Timor's** former governor to just three years in jail for failing to prevent violence during the then-Indonesian province's independence vote in 1999. East Timor's police chief was acquitted.

North and South Korea agreed to hold a series of meetings on improving economic and community ties, although no dates were set for military talks. North Korea announced separately that it will meet Japanese officials next week to discuss the re-establishment of diplomatic links.

See article: North Korea

A **Hong Kong** court found 16 Falun Gong members guilty of causing a public obstruction during a demonstration.

Europe under water

Getty

Torrential rain caused widespread flooding in central Europe. Prague's historic centre survived, just, as the river Vltava rose to its highest level since 1890. In southern Russia, some 60 people died as flash floods from the hills struck Black Sea resorts.

See article: Floods hit Central Europe

Mat Herben, leader of the **Netherlands'** eccentric Pim Fortuyn party, resigned.

Spain's main political parties agreed to start the process of banning Batasuna, the political party of ETA, the Basque-separatist terrorist group. This followed a bomb in a seaside resort that had killed a man and a six-year-old girl.

See article: Banning Spain's pro-terrorist politicians

In **Hungary**, parliamentary investigations set off by revelations that the social-democratic prime minister, Peter Medgyessy, had worked with the intelligence services in communist times, turned up evidence showing that ministers of previous governments, right and left, did so too.

See article: Hungary's politicians

Nigerian inadequacies

AP

Citing **Olusegun Obasanjo's** "monumental inadequacies", Nigerian MPs gave the president two weeks to resign or face impeachment. The dispute centres on the budget. The president proposed a highly inflationary one, full of waste. Parliament passed another budget that was even worse. Mr Obasanjo ignored it, unconstitutionally.

Following a peace deal between Congo and Rwanda, Zimbabwe's president **Robert Mugabe** said he would withdraw his country's troops from Congo, where they were sent four years ago to defend the Congolese government. He gave no timetable.

Palestinian factions agreed a draft document outlining the aims and means of their uprising, including a state in all the West Bank and Gaza. Hamas initially approved the document, but then presented amendments.

See article: Israel and the Palestinians

A popular West Bank leader and possible successor to Yasser Arafat, **Marwan Barghouti**, was charged in an Israeli civilian court with murder and membership of a terrorist organisation. Mr Barghouti has denied the accusations, saying he was a political leader who sought peace.

Amram Mitzna, the mayor of Haifa and yet another former general, announced his candidacy as leader of Israel's Labour Party. He came top of a poll of Labour voters, perhaps signalling Israelis' urgent desire for change.

Iran's president, **Muhammad Khatami**, visited Afghanistan, the first visit by an Iranian head of state for 40 years. Mr Khatami, offering money and university scholarships, said his government was extraditing people on the slightest suspicion of their involvement with al-Qaeda.

In the run up to the Johannesburg summit on sustainable development, a group of researchers sponsored by America's National Science Foundation reported on the existence of a huge "**brown cloud**" of pollution over the Indian Ocean. The cloud, a mixture of domestic and industrial emissions and smoke from forest fires, may alter the local climate and damage ocean productivity by killing plankton.

Emergency measures

After a mortar attack on Bogota by FARC guerrillas that killed 20 people, **Colombia's** new president, Alvaro Uribe, declared a limited state of emergency. He used this to decree a wealth tax to finance extra army and police recruits, to set up a new auxiliary security force, and to order new measures to intercept phone calls and to confiscate drug-traffickers' assets.

See article: Colombia cracks down on terror

Mexico's president, Vicente Fox, cancelled a trip to meet George Bush at his Texas ranch in protest at the execution of a Mexican convicted of murdering a Dallas policeman. Texas's governor had rejected a plea from Mr Fox not to apply the death penalty.

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Business this week

Aug 15th 2002
From The Economist print edition

Troubled Vivendi

Vivendi Universal unveiled losses of *euro*12.3 billion ($11.0 billion) in the first half of 2002, after writing off impaired goodwill to the tune of *euro*11 billion and making provisions of *euro*3.4 billion. Standard & Poor's downgraded Vivendi's credit rating to junk status; its shares fell sharply.

Rupert Murdoch's **News Corp** lost $1.7 billion in the quarter to the end of June after writing down the value of its stake in Gemstar-TV Guide International, pushing losses for the year to $6.3 billion. However, Mr Murdoch said that he detected some signs of an end to the global advertising slump.

See article: News Corporation's relative good health

Air turbulence

Restructuring loomed for America's loss-making airlines. **US Airways** fell victim to a combination of high costs, economic malaise and the September 11th attacks. America's sixth-largest airline filed for Chapter 11 bankruptcy protection. Capacity cuts and job losses are set to follow.

United Airlines saw its shares plummet in the wake of the fate of US Airways. America's second-largest airline admitted that it may file for Chapter 11 later in the year if it is unable to slash costs.

American Airlines announced its reaction to a persistent dearth of fliers. It will cut capacity and lay off 7,000 staff, some 6% of the total, by March 2003 as part of efforts to save over $1 billion a year.

See article: Airlines in America

Company doctor

De Beers joined a handful of companies, including Anglo American, in helping its African employees with AIDS. The South African diamond cartel agreed to pay 90% of treatment costs for the 12% of its 11,000 South African employees and spouses who may be infected with HIV.

In a wider efforts to mitigate the economic impact of **AIDS** Johannesburg's stock exchange considered proposals which would require firms to disclose HIV-infection rates among employees and their measures to combat the disease as a listing requirement.

See article: AIDS in Uganda

Representatives of **Anglo American** and **De Beers** held talks with senior South African cabinet ministers on how to get more black ownership in the industry. A leaked document had suggested that the government wants 51% of mining operations in black hands within ten years.

Bank balances

UBS Switzerland's biggest bank, beat expectations by announcing that its profits had fallen by just 4% in the second quarter, compared with a year ago, to SFr1.3 billion ($815m). **Credit Suisse**, a smaller and

poorer bank, suffered losses of SFr579m, sparking talk that UBS might try to snap it up. UBS dismissed the idea.

Allianz, Europe's leading insurer, revealed the extent of losses at **Dresdner Bank**: a first-half loss of over *euro*1 billion ($980m). Dresdner's woeful performance and its drain on Allianz's profits reignited criticism of Allianz's *euro*24 billion purchase of the bank last year.

See article: Allianz's trouble with Dresdner Bank

Reliable accounts?

Hundreds of America's chief executives and chief financial officers were required to **swear oaths** that their latest annual and quarterly reports contained no “untrue statement” nor omitted any “material fact”. A comfortingly modest number missed the deadline or restated earnings. AOL Time Warner certified its results, but admitted to revenue overstatements. The new Sarbanes-Oxley act will require many more bosses to certify regularly.

See article: Corporate America

Members of the Financial Services Forum, including some of Wall Street's biggest names, such as Goldman Sachs and AIG, joined a growing band that will treat **stock options** as expenses. The decision to act as a group may put pressure on regulators to develop a standard for treating options in company accounts.

Multinational values

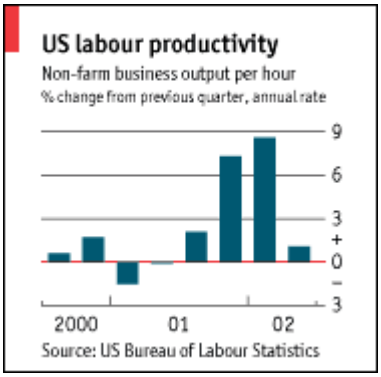
UNCTAD struck fear into the heart of anti-globalisers with a report that 29 of the world's 100 top economic entities—measured in value-added terms—were **multinational companies**. ExxonMobil ranked highest at 45th, narrowly ahead of Pakistan; BT, in 100th place, was level with Syria. But the balance of power has hardly shifted: the top 50 multinationals contribute 2.8% to world GDP, a shade less than ten years ago.

No cut, yet

The Federal Reserve failed to respond to growing clamour for a cut in **interest rates** but acknowledged the economy's weakness with a change of “tilt”, an indication that it may cut rates in the future.

See article: Greenspan keeps his nerve

In a further sign that **America's economic recovery** may be faltering, productivity, often the cause of optimism, grew by just 1.1% in the second quarter at an annual rate. It grew by 8.6% in the previous quarter. Last year's estimated productivity growth was revised down from 1.9% to 1.1%.



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Corporate governance

I swear...

Aug 15th 2002
From The Economist print edition

Oaths are only a small step in the business of cleaning up American companies

THIS week, hundreds of chief executives and chief financial officers at the biggest American companies have undertaken a curious task. They have sworn in front of a notary that, "to the best of my knowledge", their latest annual and quarterly reports neither contain an "untrue statement" nor omit any "material fact" (see article). Some goody-goodies such as ExxonMobil, Oracle and Federal Express rushed to get their oaths in early. Others waited until the last minute.

More is to come. The oath is a one-off, but the Sarbanes-Oxley act, rushed into law at the end of July, will require many more chief executives and CFOs, including (to their irritation) foreign companies quoted in New York, to certify at regular intervals that both their reports and their financial statements contain no untruths and omit no material facts.

As a way of reassuring a sceptical public that chief executives are truthful, all this has a certain primitive charm. Voters, in the run-up to the midterm elections, certainly feel a sense of primitive fury. Every week seems to unearth another bunch of beasts in the boardroom who have made fortunes while destroying much of the value of the nation's mutual funds and 401(k) pension schemes. A troupe of grotesque characters have convinced many investors that company bosses are a greedy and dishonest bunch: Linda Wachner, say, now suing Warnaco, the company she bankrupted, to be treated as a preferred creditor for a multimillion pay-off, or Dennis Kozlowski, who extracted the cost of a $6,000 gold-and-burgundy floral-patterned shower curtain and much, much more from the unfortunate shareholders in Tyco.

An oath, with its touch of mediaeval mysticism, certainly concentrates the mind. And it narrows the legal loophole that has allowed chief executives such as Jeffrey Skilling of Enron and Bernie Ebbers of WorldCom to protest that they had no idea—no *idea*—that their finance chaps were fiddling the figures. Given that a fifth of CFOs have apparently said that their chief executives had put pressure on them to misrepresent their results in the past five years, this stretches credulity.

Something must be done

However, if the Skillings, Ebberses and their sort didn't know what was going on down in the finance department, they certainly should have done. After all, accounting fraud is already a crime. Indeed, the very suggestion that the 950 or so bosses making these new declarations might previously have allowed their firms to publish reports that—to the best of their knowledge—contained untrue figures or omitted material facts ought to alarm investors, not calm them. If this is the true state of things, something more radical is needed. Yet the danger is that this week's oaths and Sarbanes's certificates may create the impression that enough is now being done.

The main impact of certification is likely to be the establishment of a paper trail, to show that top brass has signed off on reports and accounts. Other aspects of the Sarbanes-Oxley legislation will matter more, such as the act's ban on subsidised personal loans to top executives and its insistence on prompt disclosure of share dealings to repay company loans. Most important are likely to be proposals that toughen the audit process, such as the insistence that accountants rotate the audit partner overseeing a firm's accounts and that auditors can no longer sell certain non-audit services to audit clients.

The new five-member board to oversee the accounting industry is also potentially powerful—as long as it acquires members of the calibre of Paul Volcker, a former chairman of the Federal Reserve Board, and Chuck Bowsher, a former Comptroller General, rather than a pack of industry poodles. Auditors have too often chosen to ignore skeletons in corporate cupboards. A forthcoming survey by *CFO*, a sister magazine of *The Economist*, finds that auditors had challenged practices at 38% of respondents in the past year—but that in 57% of cases, the company persuaded the auditor to accept the questionable practice. That is too many for comfort.

Yet audit reform, although crucial, is not enough. Too little in the new legislation will change behaviour. The desire to take action fast has resulted in missed opportunities. As Nell Minow, a corporate activist, likes to point out, federal law has much less to say on the duties of company boards than on day-care centres. Here was a missed chance to encourage states to compete to protect shareholders' rights with light but effective rules, by allowing shareholders, rather than executives, to pick the state in which a company is incorporated.

Here too was a missed chance to make it easier for shareholders to put up candidates as board directors, and thus discourage powerful chairmen from choosing their suppliers and golfing chums for the job. That would prevent the sort of thing that happened at Tyco, whose compliant board granted Mr Kozlowski a contract saying that conviction for a felony that did not directly injure the company would not be grounds for dismissal. And here was a lost chance to infuse real transparency and meaning into the role of institutional investors, by insisting that they disclose their proxy votes. That would discourage behaviour such as that of Deutsche Asset Management, which had a business relationship with Hewlett-Packard and switched its vote on the HP-Compaq merger in HP's favour at the last minute.

Quick legislation is usually bad legislation. The Sarbanes act may be better than most. But its impact will be mild, compared with two other forces. One is that of example. White-collar crime rarely results in prison, still less in long sentences. Simply seeing a few CFOs go, handcuffed, to court has already had an electric effect in corner offices. The other is that of investors. It was investors, with their relentless hunt for double-digit earnings growth, who encouraged executive fiddling in the final years of the stockmarket bubble. Now, when some companies have decided to treat stock options as expenses, the value of their shares has risen. Others have acquired new executives who boast of their integrity. If the market comes to admire honesty, transparency and good corporate governance, executives will rush to acquire those characteristics. Even in morality, the market rules—in the end.

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Surveillance and privacy

Go on, watch me

Aug 15th 2002
From The Economist print edition

People are voluntarily surrendering their privacy

GEORGE ORWELL got it wrong—thank goodness. In the developed world, it is not the state that has ushered in a "Big Brother" society but society itself. Every day, people are adopting new technologies that trade a small amount of their privacy for greater convenience and security: credit cards, smart cards in electronic tollbooths, customer loyalty cards, cash-withdrawal machines, and "cookies" on computers. As for surveillance cameras, they have become so widely accepted that they have bred a genre of mass entertainment in the form of so-called reality TV, some even using Orwell's phrase. In all these respects, it is individuals that are deciding to sacrifice privacy in exchange for something they want more. But are there hidden costs, that society as a whole ought to worry about? After all, if governments were to suggest the use of some of these technologies, there would be a public outcry.

Where the public wants security, the willingness to give up privacy is powerful. That bodes well for the companies hoping to sell personal location technology to people who want to monitor the movement of their pets and loved ones (see article). Worries about child abductions, for example, mean that people are likely to welcome such devices. Here, the loss of privacy is fairly clear, although they may raise tricky policy questions in future—such as, at what age does your unruly teenager have the right to remove her tracking chip?

But the loss of privacy may be less obvious where people trade privacy for convenience. For example, later this year, a smart card will be introduced to bring about cashless travel on London's underground, buses and train services. Few of the 20m who use the capital's underground will realise that the card, which will work from inside a wallet or bag, will record their daily movements for billing purposes. Mobile-phone companies hold data on an individual's calls and movements. Shops hold details of purchases. Such companies frequently bleat that personal data is secure and inviolable. Yet the police, tax authorities and security services can usually gain access to such data to pursue an investigation or prosecution.

I know what you did last night

At the very least, data needs better protection from outside hackers and from those insiders with access to it. The Federation of American Scientists reasonably argues that potential abuses of data-collection systems can and should be anticipated and prevented. All data banks should have big penalties for unauthorised uses, as well as an oversight system such as an ombudsman or public review board.

However, some think the toughest questions concern the minority who choose not to relinquish privacy for convenience or security, or to those who do not have that choice—such as illegal immigrants. Everyday life is already made harder for those who do not qualify for a credit card. If basic services become inaccessible to people who choose not to (or cannot) carry a credit card, smart card or mobile telephone, say, there could be protests and other political pressure.

Such concerns, however, will weigh little on the many who feel that they have nothing to hide. If the price of freedom is inconvenience and insecurity, the truth is that most people would welcome these sorts of Big Brother. Paradoxically, only government, setting self-denying rules on the extent to which its

agencies can use personal data gathered commercially, can protect civil liberties from an Orwellian fate.

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Latin America's politics

A backlash against the free market?

Aug 15th 2002
From The Economist print edition

It's not that simple. Latin Americans just want governments that perform

AP

A FEW years ago it was confidently asserted that Latin America had turned its back on its tradition of political authoritarianism and economic populism, and was firmly set on a new course of democracy and free-market reform. Now, as economies throughout the region stumble, it is being just as confidently asserted that Latin America is turning again, back to its bad old ways. And why shouldn't it, given the failure of either democracy or the free market to deliver the political progress and economic reform Latin Americans crave?

In fact, this is a caricature. It is true that the average Latin American has many reasons to feel angry. The Argentine economy is in ruins and Brazil's finances in disarray. This follows several years of mediocre growth and rising poverty in many countries. Much of the region is emerging only uncertainly from recession. Many of the vaunted new democracies are riddled with corruption, and weakly led. But it is just too simple to blame all of this, as many do, on the supposed failure this past decade of the region's experiment in “neoliberal” economics. For one thing, there has been no such experiment; none, anyway, as uniform as the caricaturists say.

Take two examples. Chile is one of the region's more successful economies. But it has kept a giant copper firm in public ownership and was slow to relax curbs on the right of foreigners to buy shares in Chile's firms. In Brazil, President Fernando Henrique Cardoso has pursued a social democratic policy, not a “neoliberal” one. Government spending in Brazil accounts for around 40% of GDP (compared with 33% in the United States), and spending on education and health has risen.

Nor is it self-evident that the region is responding to recent failures by lurching to the left. Rather, there is a tendency, natural in democracies, to elect the opposition when governments fail. Even then, none of the demagogues vying to lead stricken Argentina looks like a shoo-in. Mexicans have plumped for Vicente Fox, best described as a Christian democrat, and Colombia for Alvaro Uribe, a conservative Liberal.

It is true that a moderately left-wing candidate (Lula da Silva), and one who is sometimes described as populist (Ciro Gomes), head the opinion polls for Brazil's October presidential election. The next president may tinker with industrial policy, through selective tariff protection and subsidised credit. If the new IMF loan fails to calm investors, he may also face a choice between defaulting on the public debt and reducing its value through a burst of inflation. But in the main no new president is likely to stray far from present policies.

Indeed, nowhere in the region does there exist a mass movement calling for a return to the state-led economic nationalism that characterised the populists of Latin America's past, such as Argentina's Peronists. Nor is one likely to emerge. In Venezuela, Hugo Chavez, who claims to be resisting “savage neoliberalism” (yes, it bites) by means of “Bolivarian revolution”, has made a poor fist of running his country, but even he has continued to privatise state firms and steered clear of capital controls. Besides, the region's old-style populists came from the right, not the left, and appealed to a far less educated electorate than that of today.

A new poll by Latinobarometro (see article) finds the average Latin American slightly right of centre, interested mainly in electing governments that work. Privatisation has certainly become unpopular across the region, but that may be because so many privatisations have been marred by corruption or have

merely transformed public monopolies into private ones. Where they have been well regulated, as in Chile and (mostly) Brazil, they have delivered better and cheaper services.

None of this is to deny that after a wretched half-decade much of Latin America is in need of a set of policies capable of generating growth. But there is little sign that its people think they can achieve this by harking back to the failed policies of the past. This, at least, is a source of comfort. Nor, yet, is there much evidence of a retreat from democracy. Building democracy amid poverty is not easy; in some places, it might still break down. But Latin Americans are learning to separate the performance of their governments from the desirability of democracy itself. That, too, gives modest grounds for hope.

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Health care in poor countries

Cheap cures

Aug 15th 2002
From The Economist print edition

Donors should give more, but the poor should spend what they have more rationally

AP

YOU can't put a price on human life. From this truism springs one of the most harmful delusions of the modern world—that when public money is spent on life-saving medical care, no account should be taken of the cost. Given that demand for health care is almost infinite, while budgets are sadly finite, it makes sense to start by spending money on interventions that save a lot of lives, cheaply. If good public health is the goal, treatments that save fewer lives at greater cost should receive lower priority.

This may seem stunningly obvious, but it is rarely practised with much rigour. In poor countries, the consequences can be calamitous. When health spending is as little as $10 per person, per year, as in much of sub-Saharan Africa, and the government blows half the budget on a fancy new hospital in the capital, this may mean that rural clinics, which serve a much larger and needier population, run out of cheap, life-saving drugs. Irrational budgeting kills.

Health-care systems have long been vulnerable to capture by elites. In Europe, the middle classes get more out of nationalised health services because they are pushier than the poor. In the same way, the much smaller elites in poor countries make sure that health budgets are spent disproportionately in cities, and on expensive, high-tech fixes for rich people's ailments, such as cancer and heart disease.

A recent experiment in Tanzania illustrates how quickly public health can improve when budgets are spent more rationally (see article). In a large rural area, researchers took the trouble to find out which diseases caused the most death and disability. They discovered that the amount of public money they had been spending to fight each condition bore no relation to the burden it imposed on the population. So, with a tiny extra infusion of cash (only 80 cents per person, per year), they redirected money towards the diseases that caused the most suffering but were cheapest to treat. Infant mortality then fell by an amazing 28% in a single year.

Following the Tanzanian model

Not all developing countries will be able to achieve such dramatic results. The starting point in Tanzania was that one child in ten was dying before his first birthday, so there was plenty of room for improvement. In, for example, much of Latin America, improvements will come more slowly because health budgets are less distorted to begin with. Over the past two decades, reforms have directed resources away from the middle classes and towards primary care for the poor, with encouraging consequences. At the other end of the scale, some countries, including several of Tanzania's neighbours, need to end their civil wars before they can rebuild, let alone reform, their health-care systems.

Despite these caveats, most governments could save many more lives by spending their health budgets more sensibly. By and large, they should focus more on low-tech treatments, not just on high-tech ones.

This idea will have many opponents. Politicians will argue that it is tantamount to telling poor countries to remain technologically backward. Aid donors, who should support it, have generally failed to do so in the past. Too often, they have paid more attention to glamorous diseases with high-tech treatments than to mundane ailments that can be dealt with more simply. For example, a large chunk of aid is earmarked for fighting AIDS, in part because defeating this scourge is a noble cause, but also because fashionable

people still die of it in the West, and fashionable people are loudly involved in the campaign to jostle western pharmaceutical firms into lowering the price of complex antiretroviral drugs for AIDS sufferers in poor countries. That is well and good. But do not neglect cheap, unglamorous life-savers, such as rehydration salts to stop children dying of diarrhoea, and bed-nets to keep malarial mosquitoes at bay.

Cheap and cheerful applies to medical personnel, too. Many developing countries spend too much training specialists, and not enough on nurses and paramedics. In countries such as Ghana, one of the biggest health-care headaches is that many doctors and nurses emigrate in search of fatter pay packets in rich countries, some of whose governments actively poach them. Paramedics, who can handle most cases, are cheaper to train than doctors, and less poachable, too.

No matter how efficiently it is spent, $10 a head will never be enough to buy adequate health care. Poor countries will eventually need to spend at least $30-40, by one reputable estimate, which is beyond most African countries' means. Since last year, rich-country donors have pledged $2.1 billion to a body called the Global Fund to fight AIDS, tuberculosis and malaria, which would help, but only around $300m has so far materialised. Donors should be more generous. Poor countries, meanwhile, should reassure them that they will give priority to scaling up the most effective interventions. A good start would be to carry out the kind of surveys that told rural Tanzanians which diseases hurt them the most. Evidence can often be the best medicine.

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British insurance

Too much of a good thing

Aug 15th 2002
From The Economist print edition

Should British insurers be forced to invest less in equities?

WARREN BUFFETT, the head of an insurance-heavy conglomerate, likes to quote Mae West, who famously maintained that you cannot have too much of a good thing. That's just how British insurers saw it during the 1990s. As the stockmarkets rose, British insurers put more and more of their assets into shares. On average, half their assets are now in equities; some insurers are 80% in equities. As stock prices rose, so did the value of the insurers' assets; and the bigger their assets, the more they grew by taking on new, riskier business. Their shareholders thought this strategy was just fine, and during the bull market Britain's life insurers outperformed not just the British stockmarket but also insurers in countries such as America where regulations prevent them from investing heavily in equities.

Now British insurers are feeling the consequences (see article). Royal & Sun Alliance's shares have lost three-quarters of their value since the beginning of the year; shares in Aviva (formerly CGNU) have fallen by 40% in the last eight months. Policy-holders are also paying the price. Rates for some of the insurance that employers are legally required to buy have risen six-fold. Life insurers have reduced payouts and imposed hefty penalties on those who try to cash in their policies early. Some life businesses, such as Equitable Life and, more recently, Royal & Sun Alliance, have closed for new business.

None of this should much concern anybody other than the insurers' shareholders, customers and an increasing number of lawyers, were it not for a broader worry. One consequence of the insurers' enthusiasm for equities is that they now own about a quarter of the British stockmarket. That makes them the largest single group of investors in British shares. If they are forced to sell equities *en masse*, they could push down the whole market, which would further depress the value of their assets, and so on downwards. The lower the market, the greater the risk. Analysts at Schroder Salomon Smith Barney, an investment bank, estimated in a recent report that if the FTSE 100 remains below 4,000 for a sustained period, about one-quarter of British life-insurance funds would be in trouble. If it were to remain below 3,600 for some time, about three-fifths would.

Some governments, worried about this systemic risk, regulate the way insurers invest. In Germany, for instance, insurers are allowed to invest only 35% of their assets in shares. In Canada, the threshold is a tenth. In America, as a result of regulation, life insurers invest on average a mere 4% of their funds in equities.

Boring is best

Should Britain adopt such regulations? Probably not. Regulations often have unintended—and adverse—consequences. One result of America's rules is that American insurers are heavily invested in corporate bonds, which has exposed many of them to the troubles of companies such as WorldCom, Kmart and Dynegy.

What's more, there should be enough flexibility in Britain's existing regulatory regime to allow the Financial Services Authority to stave off the risk of fire-selling of equities. The FSA can relax the statutory

solvency requirement for insurers—the “resilience test” which is intended to ensure that insurers have enough assets to cover their liabilities—if it is worried about the markets. The resilience test has already been relaxed three times in the past year, and there is room to relax it further.

It is managers and investors, not the government, who should learn from the insurers' troubles. Companies whose businesses require them to pay out regular, large amounts of cash should keep a good chunk of their assets in something less volatile than equities. A short-term rise in the value of your assets, way above the long-term return, does not mean you should increase your liabilities by taking on lots of dodgy new custom. Insurance is a boring business, and should stay that way.

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About sponsorship

Letters

Aug 15th 2002
From The Economist print edition

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Making states accountable

SIR – You are to be commended for your coverage of corruption in Kazakhstan ("The rot in Kazakhstan", July 27th). I would like, however, to clarify the nature of "Publish What You Pay", the proposal I support and to which you refer.

I am not calling for energy and mineral companies to agree on a voluntary "code of conduct" but rather for regulations that would require these companies to disclose net payments to entities in developing countries as a condition of being listed on major stock exchanges. Such disclosure would not solve the problem of corruption in resource-rich developing countries. However, it would empower the citizens of those countries to hold their governments accountable for the use of state revenues obtained through resource extraction and promote improved governance of state income. "Publish What You Pay" is supported by a growing coalition of more than 60 international NGOs.

George Soros
New York

Don't rubbish recycling

SIR – Your article about New York city's recycling programme focuses almost exclusively on its costs in the context of New York's fiscal crisis ("Waste of time", July 6th). While the challenges in New York are daunting, the 9,700 communities in America with kerb-side recycling programmes are making considerable progress in providing this relatively new public service in the most cost-effective manner possible. The national recycling rate for 2000 was 30%, a couple of percentage points up from the year before—still a positive sign. The Environmental Protection Agency's "Innovations Blueprint on Recycling, Retail and Resource Recovery" is designed to raise the recycling rate to at least 35% by 2005.

Citizens strongly support this programme because they understand recycling's many positive attributes, including conserving natural resources, reducing pollution and preserving disposal capacity. Recycling is also an engine of economic development. A recent analysis of the recycling and reuse industry in America found that it employs over 1.1m people and brings in over $236 billion in annual revenues. While these benefits do not necessarily translate into direct economic advantages for the local communities where materials are collected there are significant national and global benefits, both environmental and economic, from recycling.

Christine Todd Whitman
Administrator
Environmental Protection Agency
Washington, DC

View across the strait

SIR – Your interpretation of the situation between Taiwan and China is oversimplified and misleading ("Full of sound and fury", August 10th). In the past two years, President Chen Shui-bian showed moderation towards China and the Chinese leadership reciprocated with a softening of its positions. China allowed members of the legislature representing Mr Chen's Democratic Progressive Party to visit the mainland recently and relaxed conditions for negotiations about direct communications. Even China's

response towards Mr Chen's call for a referendum on Taiwan's sovereign status has been remarkably muted.

Many polls in Taiwan have shown that the majority of the population favour maintaining the status quo rather than immediate reunification with China or a declaration of independence. Mr Chen realised that his record on the economy did not warrant his re-election and took the easy way to attract votes. However, it is reckless and irresponsible for a sitting president to provoke a powerful neighbour in an appeal for the votes of an extreme minority. An international newspaper like *The Economist* should not encourage such dangerous acts.

Fred Li
Taipei

Friends of the Boss

SIR – I count myself as a liberal-minded fellow and would usually raise nary a whimper at your challenging ideologies, both secular and religious, but Lexington (August 3rd) goes too far. Bruce Springsteen “corny”? His music “a little schmaltzy”? Shame on you. Castigate, if you will, the religions of the world but question not the faith of its people.

Nick Wills-Johnson
Perth, Australia

SIR – Lexington informs us that the “best song” from Mr Springsteen's new album is “You're Missing”. It is hard to know which is worse: a political journalist telling me what rock music is best or a rock musician telling me what politics is best.

Andrew Tait
Leiden, The Netherlands

Hit by the Rock

SIR – The Treaty of Utrecht, giving Gibraltar to Britain, was unequal (“In defiance of democracy”, August 3rd). It was not a commercial transaction; Spain had just suffered a bloody war. Britain retained the Rock because of its strategic situation. Today, with satellites and NATO membership for both Spain and Britain, this should not be so important.

Agreed, Gibraltar's people (like those in the Spanish cities of Ceuta and Melilla in North Africa) should be free to choose their future. The problem is that Gibraltar's future is based mainly on activities damaging to Spain. No doubt many of Gibraltar's businesses practice legal activities but some of the 75,000 companies registered there specialise in tax evasion and drug trafficking. Many others survive thanks to the special no-tax regime of the territory. Britain has created a monster. Now we have an opportunity to dismantle it. After September 11th there are no untouchable rights for dubious business models.

Alejandro Vigil
Madrid

The price of happiness

SIR – The question is not whether money can buy happiness but how much money it takes (“Subtract rows, add sex”, July 27th). Paul Samuelson, in his famous economics textbook, presents an equation: happiness equals consumption divided by desire. At first glance crassly materialistic, this equation can also describe Buddha-like levels of serenity. Reduce your desire to zero and happiness becomes infinite.

Similarly, I derive great happiness from the assertion that it would take £170,000 ($260,000) a year to offset the loss of well-being my wife might suffer should I leave her a widow. In net-present-value terms this amounts to about £3m. Since my various life-insurance policies and other assets are worth only a small fraction of this sum, I go to bed easily, knowing that she has no incentive to murder me in my sleep.

Charles Krakoff
Amman, Jordan

SIR – If marriage yields £60,000 of happiness a year and widowhood deducts £170,000, then it is indeed far worse to have loved and lost than never to have loved at all.

Ross Frisbie
Philadelphia

Correction: A letter in the edition of June 22nd from Muhammad Yunus of Grameen Bank contained a phrase saying that the bank was "audited every two years by an audit firm of international repute". In fact, this should have said that it was audited every year by two internationally reputed audit firms.

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Health care in poor countries

For 80 cents more

Aug 15th 2002 | MOROGORO
From The Economist print edition

TEHIP

Even a tiny health budget, if spent well, can make a difference

A SMALL Tanzanian child started to shake uncontrollably. Fortunately, she was in a clinic, where the doctor guessed immediately that she was in the grip of malarial convulsions. Unfortunately, her mother believed that the convulsions were caused by evil spirits, and that if the doctor gave her daughter an injection to calm her, those spirits would escape through the needle-hole and possess more victims. So she swept her daughter up in her arms and ran out of the clinic.

The clinic staff were horrified. They knew that, if the child was taken back to her village, she would be subjected to the traditional “cure” for convulsions: she would be placed under a blanket, and made to inhale the smoke from burning elephant dung until she passed out. This would probably not address the underlying cause of her sickness, namely the millions of malarial parasites cavorting in her bloodstream. So they chased after the mother, and persuaded her to return to the clinic by promising that her daughter would not be given an injection. Instead, they gave her a tranquilliser, Valium, via a suppository. When the shaking stopped, they were then able to give her quinine to tackle the parasites, and she was cured.

Delivering medicine to the world's poorest people is a challenge. Hot, poor places such as Tanzania have many microbes but microscopic health budgets. Dangerous myths deter many sick rural folk from seeking medical help. Even if they do seek help, it is often unavailable, for they do not have the money to pay for it, and their government rarely has the money to give it to them free. Because they cannot afford adequate health care, poor people are sick a lot of the time. And because they are sick a lot of the time, they find it hard to put in the long hours of productive labour that might make them less poor—it is hard to weave, sow or haggle when you are shivering with fever.

Last year, a group called the Commission on Macroeconomics and Health (CMH), which is backed by the World Health Organisation, called for rich nations to donate an extra $27 billion a year towards grappling with poor countries' health problems. It is an excellent idea, but there seems to be little chance that such a vast sum will actually be raised. All hope is not lost, however. A recent experiment in Tanzania has shown that a small health budget can go a long way, provided that the money is spent with care. The results are so striking that they are worth examining in detail.

Poor and sick, but hopeful

By any standards, Tanzania is poor. Last year its 35m citizens divided between them a national income of $9 billion—roughly half what Americans spent on wallpaper. Most breadwinners win bread with their bare hands. On the beach in Dar es Salaam, the main commercial city, women gather shells and grind them with crude pestles to sell as a mixer for chickenfeed. Rural livelihoods are yet more precarious, which is why the Tanzania Essential Health Interventions Project (TEHIP), a joint venture of the Tanzanian health ministry and a Canadian charity called the International Development Research Centre (IDRC), was conducted in the countryside.

Two rural districts were chosen, Morogoro and Rufiji, both to the west of Dar es Salaam, and with a combined population of about 700,000. Typically for rural Tanzania, these areas combine tranquillity and staggering natural beauty with an almost complete absence of cash. Coconut palms glisten in the morning mist, dazzling sunlight plays on green-cloaked mountains and every ten-dollar shack has a million-dollar view. People in Morogoro live much as they have since agriculture first reached Tanzania. They grow starchy vegetables. They eat them. If they produce a couple of surplus sacks, they sell them for a few shillings, which they spend on such luxuries as second-hand flip-flops.

Five years ago, annual health spending in Tanzania was about $8 a head. This figure includes an estimate for the annualised value of trained staff and buildings devoted to health care. In Morogoro and Rufiji, IDRC added $2 a head to the pot, on condition that it was spent rationally. By this, the donors meant that the amount of money spent on battling a particular disease should reflect the burden that disease imposed on the local population.

This may sound obvious, but it is an approach that few health ministries take. In Morogoro and Rufiji, no one had a clue which diseases caused the most trouble, so TEHIP's first task was to find out. The traditional way of gathering health data in Tanzania was to collate records from clinics, but since most Tanzanians die in their homes, this was not terribly accurate. So TEHIP sent researchers on bicycles to carry out a door-to-door survey, asking representative households whether anyone had died or been laid low recently, and if so, with what symptoms.

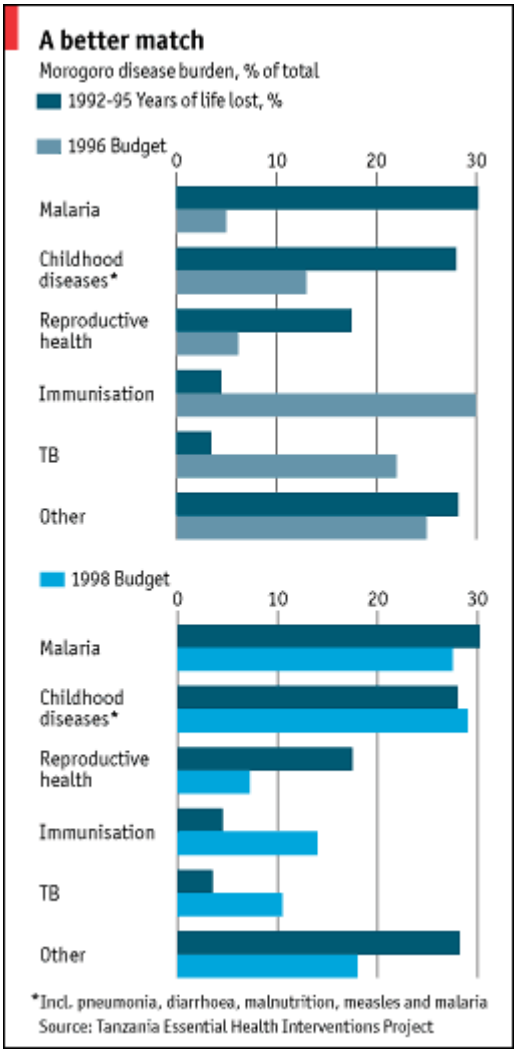
TEHIP

Cutting-edge anti-malaria technology

These raw numbers were then crunched to produce a “burden of disease” profile for the two districts. In other words, researchers sought to measure how many years of life were being lost to each disease, with a weighting to reflect the collateral damage to families when breadwinners die. They found that the amount the local health authorities spent on each disease bore no relation whatsoever to the harm which the disease inflicted on local people. Some diseases were horribly neglected. Malaria, for example, accounted for 30% of the years of life lost in Morogoro, but only 5% of the 1996 health budget. A cluster of childhood problems, including pneumonia, diarrhoea, malnutrition, measles and malaria, constituted 28% of the disease burden, but received only 13% of the budget.

Other conditions, meanwhile, attracted more than their fair share of cash. Tuberculosis, which accounted for less than 4% of years of life lost, received 22% of the budget. Vaccinations also appeared to be over-emphasised. Vaccine-preventable diseases accounted for only 4% of the total burden, but immunisation swallowed 30% of the budget.

No one wanted to scale back the vaccination programme, of course. The low incidence of vaccine-preventable disease was probably a result of successful vaccination. So there was no call to spend less on jabbing babies, but the survey did at least suggest that there was no need to spend more on jabbing them, either. Additional funds would do more good, the researchers concluded, if spent on neglected diseases for which there were cost-effective treatments or preventive measures. As it turned out, the extra $2 a head was enough to allow the district health authorities to make their spending reflect the disease burden, without trimming any successful programmes (see chart). More than enough, in fact: neither in Morogoro nor in Rufiji was the system able to absorb more than an extra 80 cents or so.



A case of algorithms

This tiny cash infusion smoothed the transition to a more effective approach to health care. Health workers, mostly nurses or paramedics rather than doctors, were given a simple algorithm to show how to treat common symptoms. For example, if a child arrives coughing, and with a running nose and a hot brow, the nurse is instructed to work through a checklist of other symptoms to determine whether it is merely a cold or something worse. If the child is breathing more than 50 times a minute, for example, he is assumed to have pneumonia, given an antibiotic and checked again after two days.

In most cases, the cheapest treatments are offered first. Children with diarrhoea are given oral rehydration salts, which cost a few cents. If the salts don't work, the child is referred to a clinic and put on a drip. For malnutrition, the first treatment offered is advice on breast-feeding. When this is not enough, cheap vitamin-A pills are prescribed. AIDS is tackled through education, condoms and antibiotics to heal open sores caused by other venereal diseases, which present the virus with an open door into a new bloodstream.

Drugs are ordered according to what is needed; previously, the government sent out the same package of pills to all dispensaries, which meant that popular drugs ran out, while others gathered dust. Non-malarial mountain villages received as many malaria drugs as mosquito-infested lowland ones, and villages where no one had ever suffered from asthma received asthma pills. “We did things blindly,” remembers Peter Nkulila, a doctor.

Perhaps most importantly, health centres in Morogoro encourage people to use bednets impregnated with insecticide, which bash mosquitoes in several ways. If the bug hits the mesh, it dies. If it merely flies close to the bednet, it feels dizzy, and either falls to earth, where it is eaten by ants, or buzzes off to rest and recuperate, which means that it will bite no one that night. A bednet's mosquito-repelling effect stretches for 500m in all directions, so netless villagers gain some protection from their better-equipped neighbours.

Conservative types at first shunned bednets in favour of the *mtuti*, a hot itchy traditional sleeping bag woven of palm leaves. But with a bit of urging from nurses, they discovered that cotton bednets are

softer on the skin and better at beating back bugs. Despite the cost—about $3 for a locally-made net, with the insecticide somewhat subsidised—the nets are popular. Village shops sell them. Peasants hang them in *shamba* huts on stilts in their rice-fields, where they sleep during harvest season, so as to be at hand to scare off crop-munching hippos. In Morogoro, even the Masai, a fiercely conservative tribe of nomadic cattle-herders, when sleeping under trees, have started draping themselves in insecticide-soaked bednets.

The results of all this were stunning. In Rufiji, infant mortality fell by 28% between 1999 and 2000, from 100 deaths per 1,000 live births to 72. The proportion of children dying before their fifth birthdays dropped by 14%, from 140 per 1,000 to 120. The figures for Morogoro are thought to be equally good, although TEHIP is still trying to confirm their accuracy. In nearby districts, and in Tanzania as a whole, there is no evidence of a similar improvement over the same period. And anecdotal evidence suggests that better health has made Morogoro and Rufiji less poor.

Fewer bugs, more bikes

Rain falls in booming cascades on Melela, a village near Morogoro. Pedestrians hold big palm leaves over their heads to keep the water off. When the downpour stops, puddles stagnate and become hatcheries for mosquitoes. As Jeffrey Sachs of Columbia University has noted, where malaria prospers, people usually do not. In Tanzania, 94% of people are at risk of catching the disease. Roughly half the population does catch it each year, and 100,000 die of it. While in the parasite's grip, people are often too weak to work. Some of their relatives must down hoes to nurse them, and spare cash in the family biscuit tin must be spent on anti-malarial drugs. “When you have a sick child in the family, you are all sick,” notes Hamza Mfaume, chairman of the Morogoro district council. Mr Sachs estimates that countries like Tanzania would be twice as wealthy without malaria. Whatever the actual figure, the people of Morogoro are sure they are better off now that the disease is being rolled back.

Mustapha Dangeni, a young peasant, recalls that his two children used to be smitten with fever almost every month before he got a bednet. Now, he says, they have been healthy for a whole year. Mr Dangeni and his wife have been able to spend more time tending their fields, so they have produced more spare maize and millet at a time when their expenditure on anti-malarial drugs is at an all-time low. With the extra cash, they have bought a radio, a bicycle and some furniture. “Things are continually improving,” says Mr Dangeni, smiling as he leans against a sack of charcoal.

A lesson for others

Could this success be repeated elsewhere? The Tanzanian government is keen that the lessons learned in Morogoro and Rufiji be applied in other parts of the country. So keen, in fact, that it is pushing TEHIP's cautious, methodical organisers to move faster than they would prefer.

Tanzania is probably one of the easiest poor countries in which to put ideas like this into practice: the country is peaceful, stable, and has a government that takes health care seriously. Almost as important, it has been steadily moving away from the highly centralised health-care system that was put in place during the country's socialist phase, which ended in the 1980s. Local people have assumed greater responsibility: in the old days, if a clinic roof blew off, they would wait for the central government to fix it, which it rarely did. Now, the nearby villages are more likely to pool their spare cash, buy some sheets of corrugated iron, and fix it themselves. In Morogoro and Rufiji, they have gone one step further, and are building their own dispensaries. This is expensive in the short term, but having a health facility nearby means that they don't have to take so many costly bus trips into town.

TEHIP

Discovering what hurts, and what works

In other countries, the lessons of Morogoro and Rufiji may be harder to apply. Neighbouring Congo and Burundi, for instance, are too preoccupied with civil war to fuss over making their health budgets more rational. Some governments have bizarre priorities: Zambia, for example, budgeted half as much money for tackling AIDS last year as for building villas for visiting heads of state. Waste is common: one study found that for every $100 of African tax revenue spent on drugs, patients received $12 of benefits. (The rest was lost through non-competitive procurement, poor storage and bad prescriptions.)

Corruption is another common hurdle, but need not be an insuperable one. It helps that the sums involved are small—less tempting to powerful crooks than larger amounts would be.

Tanzania has its share of piratical politicians, but there are no reports of TEHIP funds vanishing. It probably helps that the scheme is locally run, involves the active participation of the people who are supposed to benefit and is led by organisers, such as clinic managers, who are much more accessible, and therefore accountable, than politicians in the far-off capital city. If the head of a clinic in Morogoro filched from his budget to buy a flashy car, the locals would notice and doubtless make him regret it.

More countries should copy the Morogoro model. And donors should pay heed that, while more money is certainly needed to tackle poor countries' health problems, how it is spent is more important than how much is spent.

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Fire in the west

Another costly war that America can never win?

Aug 15th 2002 | SEATTLE
From The Economist print edition

AP

Without a radical rethink, America's forest fires will only get worse

Get article background

THE August 12th daily report from the National Interagency Fire Centre in Boise, Idaho, has a familiar ring: 167 new wildfires; dozens of large fires burning, including the biggest in Oregon's history; conditions ideal for more blazes in every western state except New Mexico (where it has finally been raining). So far this year some 5.5m acres (2.2m hectares) have been consumed in forest fires.

The fire centre in Boise, where meteorologists, fire specialists and dispatch crews try to manage existing fires and anticipate new ones, has been on its highest level of alert for nearly two months. Exhausted dispatchers are now looking to the armed forces and to Canada for help. The Forest Service will spend $1 billion this year on putting out fires—and that does not include the money spent by other agencies or the damage to property.

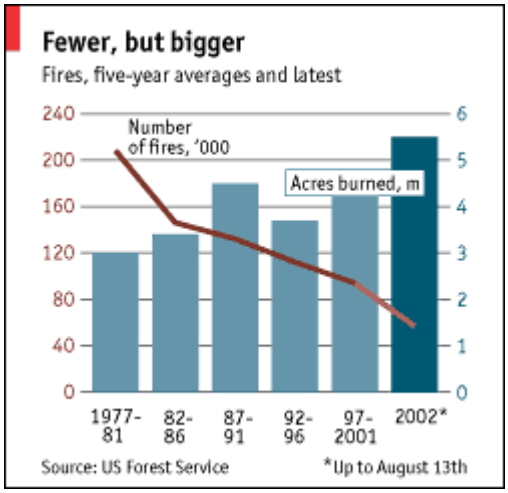
There are other costs. Fifteen fire-fighters have died this year, five of them in horrific aircraft crashes. The environmental damage is also rising. The huge Ponderosa pine forest, which stretches all the way from Mexico to Canada, is being ravaged. The habitat of creatures ranging from the Mexican spotted owl to the tassel-eared squirrel is disappearing with it.

There are a few special reasons for this year's emergency. Most obvious is the severe drought throughout most of the Rocky Mountain area, which helped make two June blazes, in Arizona and Colorado, the worst in those states' histories. But behind that is a trend towards fewer, larger fires (see chart). In the 1970s, the average fire covered 20 acres. So far this year it has been 96 acres. In 1970, a fire of 500 acres was considered extremely serious; nowadays such blazes are hardly mentioned. This year, the big fire in Oregon has eaten up 300,000 acres.

How to explain the new trend? Ironically, the answer is: not enough fires. The west's forests are meant to burn regularly and lightly. Historically, lightning provided the spark; when that failed, native Americans used to start small fires deliberately. These low-intensity fires did little damage to the big Ponderosa pine trees that dominated western forests.

All that changed in the 1880s, when settlers introduced sheep and

cattle, which ate the grasses that fuelled the fires. Without the fires, shrubs and seedlings flourished. The Douglas fir, which produces more seeds than the Ponderosa pine but is much less tolerant of drought or fire, did especially well.



In 1910, a series of enormous fires ravaged Montana and Idaho. Three years later, the head of the nascent Forest Service argued that protecting forests from fire was his organisation's "fundamental obligation". From its humble beginnings (for a while, the fire-fighting force consisted largely of drunks and vagrants) the service gradually became more professional, developing new techniques and introducing smokejumpers (special teams that parachute into hot spots). By the early 1960s big fires had almost been eliminated.

A bad policy, it turns out. Ponderosa pine forests are now dangerously dense. Worse, the forest floor is head-high with brush, making it easy for fires to leap from ground level and take hold on trees that have survived dozens of previous blazes—thus helping to create "megafires" like those presently burning in Oregon and Montana. The brush also makes it harder for the Forest Service to conduct controlled burns. One such burn got out of control in 2000, briefly threatening the Los Alamos weapons centre in New Mexico.

The fires will get worse. Wally Covington, a professor of forestry at Northern Arizona University, reckons that 75m acres of western forests are prone to severe wildfire. He recommends thinning forests back to their original density, leaving just two trees for every stump that could be found dating from around 1900 (the assumption being that some of those left standing will die). Fire could then be safely re-introduced to keep down the brush.

This is a radical, long-term solution. It is a measure of the current disaster (and its expense) that Mr Covington's scheme has actually been welcomed by officials from both the Clinton and Bush administrations. Yet there is little chance of it being put into practice.

Some of the loudest opponents to the idea of returning forests to their native state are environmentalists. Greens are suspicious of any efforts to remove trees from national forests—not least because the Forest Service has often allowed perfectly healthy trees to be logged in the guise of aiding forest health. "There just isn't much trust between groups such as ours and the Forest Service," says Bob Ekey of the Wilderness Society.

A less vocal group which plainly has no interest in reducing the number of fires is what might be called the "fire-industrial" complex. A big fire can chew up several million dollars a day; the current tab in Oregon is already $50m. Relatively little of that goes to the Nomex-clad fire-fighters shown battling heroically on the evening news. Most of them make $14 an hour, or work on a volunteer basis. The serious money goes to an entourage of private contractors, who supply everything from earth-moving equipment and helicopters to portable showers. Nine companies control a fleet of 40 fixed-wing aircraft; it costs around $6,000 an hour to rent them. The same group of people travel from one blaze to the next.

Such services are all, of course, badly needed. But their existence makes it easy for the Forest Service to stick to its reactive "big-iron" approach to fire control; and their pull on resources leaves ever less money for more mundane forms of fire prevention, such as spending $2,000 an acre to pay people to chop down overgrown trees and brush.

In a strange way, America's war against fires is similar to its war against drugs. Many lives have been lost and a great deal of money spent struggling against a fearsome enemy. But too little has been done to address the underlying causes, while a radical solution goes begging.

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The New York governor's race

Where politics really is local

Aug 15th 2002 | NEW YORK
From The Economist print edition

A logical, uncomplicated New York race? Fugeddaboudit

WHEN Tip O'Neill said that “all politics is local”, he was exaggerating. Most state elections are linked to national concerns in some way, such as prescription-drug benefits or corporate scandals. But this year's governor's race in New York is about as local as you can get.

An outsider would assume that the incumbent, George Pataki, will win a third term by a mile. A likeable moderate Republican who performed well after September 11th, he enjoys Bushesque approval ratings. He has been endorsed by some unions, including the powerful hospital workers (for whom he just helped secure a $1.8 billion pay-deal). Unlike in 1994, Rudy Giuliani will surely endorse him (the über-mayor still loathes the governor, but his future political prospects depend on him not rocking the Republican boat). Mr Pataki has raised around $30m—four times more than anyone else. And opinion polls say he will trounce whoever wins the Democratic primary next month.

But this is New York, and the race is likely to prove closer (and immensely more Machiavellian) than that, for three reasons. First, this is Democratic turf: they outnumber Republicans five to three among registered voters. In his two previous races, Mr Pataki won with 49% and 54% of the vote—hardly overwhelming victories. Second, New York's famously dysfunctional state finances—it hardly ever manages to pass a budget on time—are in worse shape than ever. Tax receipts have fallen by a fifth. Fairly or not, Mr Pataki will get some of the blame.

The third reason is the state's weird election laws. The governor's race is not a two-party affair. The Conservative Party, which last time collected 7% of the votes, will also have a candidate on the ballot paper. Usually the Conservative ticket is the same as the Republican one, so the tallies are added together. This time there is a glitch. Mr Pataki will almost certainly be the gubernatorial candidate for both parties, but Mary Donohue, his running-mate on the Republican ticket, has a rival for the second spot on the Conservative ticket: one Dan Mahony.

This is where things get complicated. Mr Mahony, who stands accused of voting twice in previous elections, has filed a petition to usurp Ms Donohue's name on the Conservative slate. Normally he might not be heard, but he has nearly the same name as one of the Conservative Party's founders, Daniel Mahoney. That means that he stands a chance of becoming Mr Pataki's running mate on the Conservative ticket. And if that were to happen, Conservative votes could not be added to Republican ones, because the two tickets would be different. So Mr Pataki could either be forced into attacking the ticket he wants to lead, or end up with wasted Conservative votes.

Mr Pataki's small-party woes do not end there. Tom Golisano, one of America's 400 richest people, has also barged on to the ballot, as the candidate for the even-tinier Independence Party, and possibly as a write-in Conservative as well (lawsuits are flying about this). He won 8% of the vote in 1998, he has a vendetta against Mr Pataki and he is perfectly willing to spend $70m on his campaign, most of it on anti-Pataki ads.

If Mr Pataki can somehow manage to finesse these wild cards, he can take great comfort from the fact that the two main Democrats, Carl McCall and Andrew Cuomo, are busy knocking each other senseless. The latest twist: Mr McCall, the state comptroller and the favoured candidate of the New York Democratic machine, has been busy attacking the last Democratic governor, Mario Cuomo, who happens to be Andrew's father.

The battle is really about race. Around 22% of the voters are black; 8% are Hispanic. Mr McCall, the first black politician to hold statewide office, hopes to win almost all the black vote and two-thirds of the

Latino vote: that means that he would need the support of more than a third of the whites to win. Mr Cuomo is hoping to win most of the white votes and pick up 40% of the combined black and Latino vote. His secret weapon: a Harlem office worker called William Jefferson Clinton. The former president has a lot of support among blacks and Mr Cuomo used to be his secretary of housing.

The plot to succeed King George

Given Mr Cuomo's pedigree (he is even married to a Kennedy), why is the Democratic machine revving up behind Mr McCall? Once again, things get Machiavellian. Most Democrats still expect Mr Pataki to win, so they are manoeuvring for 2006 (when they hope that Mr Pataki will be less popular). To everyone except Mr Cuomo, Mr McCall is seen as a perfect stop-gap candidate who will lose gracefully then retire. Bigshot Democrats can then prepare for battle at a more propitious time. Some whisper that such an outcome might not harm even Mr Cuomo too much, since he will have more time to put in work with black and Latino voters.

One obvious problem with such manoeuvring is that it hands this race to Mr Pataki. If he were a certain winner, that might be sensible. But people who assume that an incumbent is unbeatable can get caught out: ask the elder Mr Cuomo, who sat out the 1992 election only to watch Mr Clinton clobber George Bush senior.

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Kidnappings in California

Waves of fear

Aug 15th 2002 | LOS ANGELES
From The Economist print edition

A little girl is found safe and sound—as most of them are, thankfully

Get article background

AP

Jessica returns

FOR Rafael Cortez and Maria Hernandez, the statistics were irrelevant. Their four-year-old daughter, Jessica, disappeared from Echo Park in Los Angeles early in the evening on August 11th, while they sold tacos from their stand nearby. For 48 hours, until Jessica turned up unharmed at a children's clinic five miles away, they watched as police scoured the park pond to see whether she had drowned, and later turned their attention to the whereabouts of a tattooed man whom witnesses had spotted talking to the girl.

Local television stations followed the story closely. It seemed to fit a sinister pattern. Other cases in California and elsewhere in the country were cited; reporters spoke of a wave of child abduction; the wave soon became an epidemic. (Britons are seeing something similar in the coverage of the hunt for two ten-year-old schoolgirls, Holly Wells and Jessica Chapman, who have been missing, at the time of writing, for 11 days.)

The incessant talk of an “epidemic” has had all kinds of effects. Last week police stations around Los Angeles offered to take finger-prints of children so that their parents would have a record if they went missing. Gray Davis, the governor of California, launched a system known as “Amber alerts”, after a little girl who was murdered in Texas in 1996, which broadcasts information about lost children over the radio and on road signs. George Bush announced a conference to be held in September aimed at blocking the “wave of horrible violence” threatening children.

Doubtless the conference will produce ideas for better co-ordination between national and local law enforcement in tracking lost children. And California's Amber-alert system, after some early problems, has already contributed to the rescue of two Los Angeles teenagers. Similar systems in other states are thought to have helped in the rescue of 17 abducted children over the past five years. But the general alarm set off by talk of an “epidemic” is a less obvious force for good.

The only wave that has broken is one of publicity. There are 56m children in America. Very few of them are abducted by strangers, and the numbers do not appear to have grown at all in recent months. The FBI lists 62 such abductions since last October, a rate slightly lower than that of the previous year, for which it reported a total of 93 cases.

Panic about children's safety flares up regularly, usually with little relation to overall trends. The case that triggers the panic will often have some vivid resonance, like the kidnapping of Charles Lindbergh's son in 1932. Young Jessica's ordeal in Echo Park struck a different but harmonious chord with Californians; not coincidentally, it did so within one of the world's largest media markets. And the certainty that the media will always need something new to report on is the guarantee that this so-called epidemic will wane just as quickly as it waxed.

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The summit in Waco

Poor economics, well spun

Aug 15th 2002 | WASHINGTON, DC
From The Economist print edition

The president lays a trap for the Democrats

GEORGE BUSH'S forum in Waco, Texas, was a snorey. Touted as a gathering of those “on the front lines of the American economy”, the meeting at Baylor University (whose mascot is a bear) was a glorified photo-opportunity.

Newspapers wrote about how much money the invitees had given to the Republicans and mocked Mr Bush's “Message: I care” theme. Democrats in Congress, who had not been invited, complained that there weren't any serious policy discussions. Which was fair enough: the only new policy was Mr Bush's pledge not to release $5.1 billion of authorised spending on homeland security, as a token of his seriousness about restraining the budget deficit.

But one thing did emerge from Waco. The Republicans are now becoming the bullish party, and the Democrats the bearish one. At a time when many economists are downgrading their forecasts for the economy, the president blared that “we're confident in the long-term health of the economy”, and his treasury secretary, Paul O'Neill, bravely predicted there will not be a double-dip recession. Meanwhile, the Democrats are belly-aching about the slowdown and contrasting Mr Bush's economic record with Bill Clinton's.

If the economy is in miserable shape in November, the bearish party will surely do better. But the Democrats are taking a risk—and not just because the economy may improve. Sunny optimism, however misplaced, often plays better on the hustings than tormented pessimism, however justified. Mr Bush's stage-show in Waco may have had a point after all.

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Chicago

Green machine

Aug 15th 2002 | CHICAGO
From The Economist print edition

The grimy "hog-butcher of the world" may become America's greenest city

FOR most of its life, Chicago's motto, *urbs in horto*, seemed a stretch. Frederick Law Olmsted and Daniel Burnham may have laid out grand plans for the "city in a garden" a century ago. But it soon became a gritty manufacturing and railroad hub. Its factories belched smoke and its river stank. During the 21-year reign of Mayor Richard Daley, the Park District was mainly a centre for political patronage.

Over the past decade, a remarkable transformation has taken place under Daley's son. The current mayor, Richard Daley, elected in 1989, has just picked up a string of awards for achievements such as "city livability". Hardly a beard-and-sandals type, the burly Mr Daley seems to have espoused greenery simply because he thinks it makes the city nicer. To that end, he has planted some 300,000 trees over the past 13 years. The city spends $10m a year on new trees, flowers and shrubbery. Some 500 black-crowned night herons already live in a new reserve in the once heavily polluted Calumet area.

Now Mr Daley is trying to cement (so to speak) his green legacy in an ambitious Central Area Plan (CAP), guiding the development of downtown Chicago for the next 20 years. The CAP, which is now under discussion at various public hearings, is not a cheap project: the transportation bit of the CAP alone will cost around $10 billion. But the green parts are popular.

Chicago has always had one great natural asset: Lake Michigan. More than 20m people a year enjoy its lakefront parks, beaches, museums and bike paths. The CAP is devoted to expanding this still further, adding more lakefront parkland and boating space (Chicago already has the country's largest harbour system), and even creating offshore islands to attract birds and tourists.

But Mr Daley has been tidying up the inner-city too. His parks superintendent, David Doig, looks after 550 parks with an annual budget of $334m (the largest parks budget in the country). There are currently two acres of park for every 1,000 residents—and the ratio rises to four acres if you include other sorts of green space. Mr Doig wants the ratio to be five acres.

Some of the city's eyesores, however, are harder to improve—notably the Chicago River. Years of manufacturing waste lie buried in the riverbed, and the Deep Tunnel, a massive waste-water-removal project initiated in the 1970s, occasionally overflows during heavy rains, dumping polluted water into the river. Stricter dumping regulations have cleaned it up enough for the number of fish to rise, and the city is now buying land along the riverbank to extend a green corridor. But even Mr Daley's most ardent admirers would not want to swim in the murky waterway.

There are other problems too. Parts of the city are all concrete, steel and asphalt, without a blade of grass in sight. Polluted brownfield sites need to be cleaned up. The Environmental Protection Agency still puts Chicago in its second-worst category for ozone levels (though the city's overall air quality is among the best in the country for a city of its size). And Mother Nature can be unco-operative. A recent spell of hot weather has been blamed for an increase in e-coli counts at the city's beaches. It has also turned a much-touted rooftop garden on City Hall a nasty brown colour.

Grass: you can never have enough

Meanwhile, Mr Daley's very success is creating a problem: nice cities attract outsiders. The CAP reckons that the number of people living downtown and in adjacent neighbourhoods will rise from 83,500 to 138,000 by 2020.

Alicia Berg, Mr Daley's planning commissioner, denies that greenery and development is “an either/or situation”. Those parks are one reason why Boeing has moved its headquarters to the city. Donald Trump's mooted skyscraper along the river depends on the developer providing some parkland with it. But the more people that come to Chicago, the more trampled Mr Daley's parks may become.

Another problem is money. Mr Daley has been able to splurge on his beloved trees during a boom time for the city. The Park District has an independent budget, supported by property taxes, so it should be shielded from city cutbacks; but its user fees have already dipped in the economic downturn. Mr Daley wants the private sector to contribute more. Unfortunately, Millennium Park, the best known of the city's public-private projects, is vastly over budget and years behind schedule.

The final worry is that Chicago's greenery depends too heavily on Mr Daley. Kathy Madden, director of the Urban Parks Institute in New York, points out that many cities are placing greater emphasis on green space; it is Mr Daley's ability to crack the whip that has put Chicago so far ahead of the others. What if he were to leave City Hall? Mr Daley's own answer is characteristically blunt: “The trees will keep growing.”

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Georgia politics

The Middle East meets the South

Aug 15th 2002 | ATLANTA
From The Economist print edition

A House race in Georgia with a Palestinian twist

GAZA is a long way from suburban Atlanta, but the Middle East may decide the fate of congresswoman Cynthia McKinney. On August 20th, she faces a tough primary challenge from Denise Majette, a former state judge who, like Ms McKinney, is black. The election has become a sort of proxy war for the Arab-Israeli conflict. It also reflects shifting alliances between American Jews, Arabs and blacks.

Since September 11th, Ms McKinney has seemed to court trouble. Last October, she wrote to Prince Alwaleed bin Talal in an effort to relieve the Saudi prince of the $10m he had tried to donate to New York city (but which had been rejected by Rudy Giuliani because he thought the money was tainted). She then accused George Bush of having prior knowledge of the terrorist attacks and allowing them to proceed so as to benefit his friends in the defence industry. Now she is under fire for accepting campaign money from Arab groups and individuals that are suspected of supporting Muslim terrorists.

Some of Ms McKinney's utterings are, from any perspective, eccentric; but some Arab-Americans prefer to put her support for the Palestinians within the context of a broader rapprochement between blacks and Arabs. Khalil Jahshan of the American-Arab Anti-Discrimination Committee admits that in the past Arab groups have not always reciprocated offers of support from black politicians. But since Arabs now suffer tougher racial profiling, they feel more sympathy for black causes.

By contrast, black advocacy groups have long enjoyed generous financial and volunteer help from Jews—though the relationship has sometimes been fractious (both Jesse Jackson and Al Sharpton have been accused of anti-Semitism). Now some black leaders, including Ms McKinney, see Jews less as an oppressed minority in America and more as the oppressors of the Palestinians in the Middle East.

Ms McKinney's battle mirrors a June primary in Alabama, where another pro-Palestinian black Democrat, Earl Hilliard, was ousted by Artur Davis. Although local issues probably proved decisive, Mr Davis received a lot of money from pro-Israel groups. Meanwhile, Mr Hilliard's colleagues in the Congressional Black Caucus threatened to withdraw support for aid to Israel unless the Democratic leadership formally supported Mr Hilliard (which it eventually did). Another forlorn (and hypocritical) attempt to help Mr Hilliard came from Mr Sharpton, who flew down from New York to Birmingham to denounce outsiders butting into the election.

The mathematics of bashing Israel in American politics remain clear. Although Arab-Americans have given generously to both the Hilliard and McKinney campaigns, their efforts have been dwarfed by the Israeli lobby. Jewish groups have spent over $41m over ten years on political contributions, compared with the Arabs' $297,000, according to conservative estimates by the Centre for Responsive Politics. Despite being the challenger, Ms Majette has raised more than $1m, almost twice as much as Ms McKinney.

So is Ms McKinney doomed? Polls seem to indicate the candidates are in a dead heat, and Ms McKinney's support among black voters, who comprise half the electorate, is holding up well. One ominous sign: to honour the victims of September 11th, some local politicians want to rename a road Memorial Drive; it is now the Cynthia McKinney Parkway.

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Lexington

Heartbroken

Aug 15th 2002
From The Economist print edition

Is rural America really such a great role model for the nation?

THE *Financial Times* is not normally given to puffing George Bush. But on Monday it splashed a picture on its front page that, from the White House's point of view, more than made up for all those sniffy editorials about the budget deficit. A rugged-looking president is dressed in jeans and a sweat-sodden T-shirt. In his gloved hands he carries branches that he has just lopped off trees. On his head, protecting him from the searing Texas sun, he wears a white cowboy hat.

Bill Clinton spent his vacations in Martha's Vineyard, sucking up the salt air and bantering with the likes of Ted Danson. Mr Bush prefers to labour on his Texas ranch, clearing brush, chopping down trees and defying the 110-degree heat. This is a man with deep roots and solid values, the White House whispers, a man who is at home in the heartland.

Mr Bush is not the first president to repair to the heartland for reinvigoration. Teddy Roosevelt liked nothing better than trekking out west, where he slipped into cowboy regalia and slaughtered wildlife. Lyndon Johnson spent his holidays on a ranch not too far (in Texas terms) from Mr Bush's place. Jimmy Carter liked to unwind on his peanut farm in Plains, Georgia (where he once did battle with a “killer rabbit”). Even Mr Clinton was once forced to leave the beach: in 1995, with an election looming, his pollster, Dick Morris, told him that people wanted to see him hiking in the country rather than frolicking with celebrities.

Why is it deemed so important to holiday in the heartland? The centre of America certainly contains many wonderful vacation spots, but Plains, Georgia, and Crawford, Texas, are not among them. The simple reason is that Americans regard the heartland as more than just a geographical expression (the country's central and rural areas). It is a moral condition: an embodiment of the authentic American tradition of self-reliance, family values and community spirit. The inhabitants of the heartland are descendants of the rugged pioneers who carved a great civilisation out of mountains and prairies. They continue to make their living by doing proper work—by wrestling with nature rather than shuffling symbols on a screen. Mr Bush is well aware of his electoral success across “real” America, while Al Gore was left with the celluloid bits. Hence the value of that gritty picture in the FT (even if it was largely seen by stockbrokers lounging around Long Island).

But is the heartland really such an embodiment of self-reliance? Sadly, its true characteristics are not

vigour and independence but economic decline and government handouts. The small communities that are supposed to embody the American spirit are, in fact, haemorrhaging jobs, people and wealth.

The worst poverty in America is probably not in the inner cities but in the countryside—in places like Mississippi, Arkansas and Kentucky. Six of the country's ten poorest counties can be found in the area stretching from Texas (where Mr Bush is so hard at work) to California's central valley. Rural people make barely 70% of the salaries of their urban counterparts. One in six rural children is being raised in poverty.

Ever since the dustbowl of the 1930s, the heartland has been hopelessly dependent on government handouts. Last year the country spent $25 billion on direct subsidies to farmers, and billions more subsidising water, power and infrastructure. Twenty-five cents of every dollar in farm revenue comes from the government. Paul Krugman, an economist at Princeton, calculates that the “blue” states (ie, the phoney coastal ones that Democrats win) subsidise the red Republican states to the tune of $90 billion a year—and that was before the recent farm bill.

The secret of the heartland's success in securing such largesse is simple: political clout. Wyoming, with a population of half a million, has as many senators as California, with a population of 34m. Just 16% of the population elects half the Senate.

Yet subsidies are, at best, a mixed blessing. They are robbing the heartland of its spirit of initiative and entrepreneurship. Rural ghettos now suffer from all the dependence-induced pathologies of their urban cousins. They are also creating a sort of state-funded feudalism that is the very antithesis of the American tradition of rugged individualism. Huge quantities of government money flow to a handful of landowners, most of them in Texas and California, who preside over vast armies of ill-educated and poorly paid migrant workers.

If you want morality, go to the Hamptons

What about the heartland's much-vaunted moral qualities? Here again the image of small-town piety bears little relation to reality in rural America. The states that Mr Bush won in 2000 boast slightly higher rates for murder, illegitimacy and teenage childbirth than the supposedly degenerate states that voted for Mr Gore.

In recent years the worst increases in both crime and drug abuse have taken place in the heartland. In the past five years, bank robberies jumped by 82% in small towns, compared with 17% in America as a whole. Many rural communities are plagued by drugs, particularly amphetamines and OxyContin (an opiate pain-killer). In the 1990s the percentage of drug-related homicides tripled in rural areas but halved in big cities.

The true story of the American heartland is more complicated—and more tragic—than the one that the White House is trying to tell. The taming of the heartland is one of the great achievements of the human spirit (albeit one marred by the brutal treatment of the native population); it also includes plenty of straight-talking, upright, God-fearing folk of the sort that are rare in Malibu. But a combination of economic change and disastrous social policies is turning a rural idyll into a rural ghetto. A president who really cared about the heartland would devote a little serious thought to its problems, rather than just treat it as a backdrop for his re-election campaign.

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The Latinobarometro poll

Democracy clings on in a cold economic climate

Aug 15th 2002
From The Economist print edition

Latin Americans are starting to distinguish between bad governments and the benefits of democracy itself

Still doubting democrats 1

Which of the following statements do you agree with most?, %

	Democracy is preferable to any other kind of government					In certain circumstances an authoritarian government can be preferable to a democratic one				
	1996	2000	2001	2002	Change since 1996	1996	2000	2001	2002	Change since 1996
Honduras	42	64	57	57	15	14	15	8	14	0
Venezuela	62	61	57	75	13	19	24	20	12	-7
Mexico	53	45	46	63	10	23	34	35	20	-3
Nicaragua	59	64	43	63	4	14	6	22	12	-2
Uruguay	80	84	79	78	-2	9	9	10	10	1
Ecuador	52	54	40	49	-3	18	12	23	18	0
Costa Rica	80	83	71	77	-3	7	6	8	8	1
Chile	54	57	45	50	-4	19	19	19	14	-5
Argentina	71	71	58	65	-6	15	16	21	17	2
Peru	63	64	62	57	-6	13	13	12	16	3
Guatemala	51	45	33	45	-6	21	21	21	12	-9
Bolivia	64	62	54	56	-8	17	13	17	20	3
Brazil	50	39	30	37	-13	24	24	18	15	-9
Paraguay	59	48	35	45	-14	26	39	43	38	12
El Salvador	56	63	25	40	-16	12	10	10	16	4
Panama	75	62	34	55	-20	10	18	23	16	6
Colombia	60	50	36	39	-21	20	23	16	11	-9

Ranked by increase in support for democracy. Not including those who answered "It doesn't matter" and don't knows
Source: Latinobarometro

DESPITE the economic turmoil gripping many of their countries, Latin Americans are becoming somewhat more supportive of democracy, but they have little trust in political parties and believe that corruption is widespread and worsening. They have lost faith in privatisation, and want the state to take a more active role in regulating the economy, but in most countries they have not moved more generally to the left. These are the main conclusions of the latest regional poll taken by Latinobarometro, a Chilean organisation, and published exclusively by *The Economist*.

The poll covers 17 countries in the region. Latinobarometro has conducted similar opinion surveys regularly since 1996, so the poll is good at capturing changes in opinion over time, and between countries.

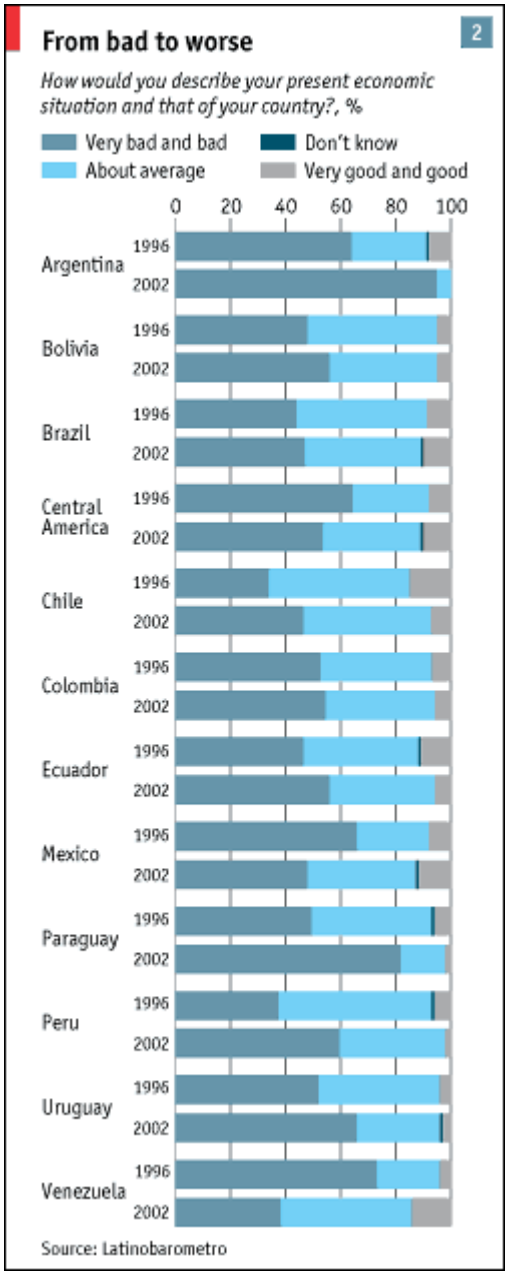
What emerges is a ray of faint hope for democrats. In 14 countries, support for democracy increased over the past year, in some cases substantially (see first illustration above). In some cases, that is because elections have brought to power new political groups (Mexico in 2000) or seen the ejection of a reviled

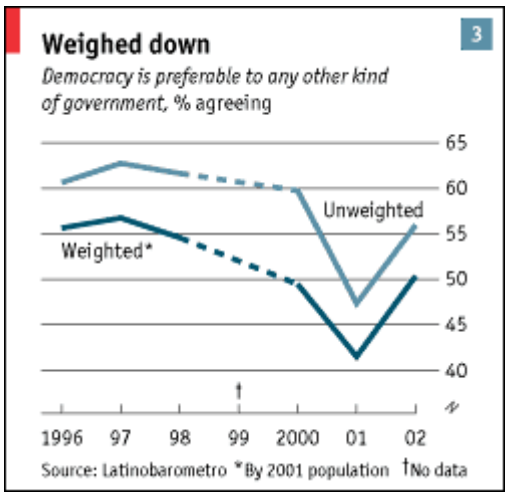
president (Nicaragua). In Venezuela, both supporters and opponents of President Hugo Chavez (who survived a coup attempt a fortnight before the poll was taken) seem to take democracy as their banner. Elsewhere, support for democracy may have bounced back in line with a slight improvement over the past year in how Latin Americans see their economic situation.

But such support still remains worryingly low in some countries, such as Brazil and Colombia. And in all but four countries, it is lower today than it was in 1996, probably because of Latin America's generally poor economic performance in recent years (see chart 2). When the poll results are adjusted to take into account the countries' populations, they suggest that only 50% of Latin Americans are convinced democrats (chart 3 below). And most remain deeply dissatisfied with the way their democracies work in practice, though in 12 countries their discontent has diminished since 1996 (chart 4 below).

Even so, overall, support for authoritarian government is not increasing (and in Brazil, Colombia and Venezuela it has declined significantly). Only in Paraguay has it increased substantially since 1996; even there, last year's majority in favour of authoritarianism has been reversed.

Perhaps the most striking result is from Argentina. Notwithstanding the collapse of the country's economy, support for democracy there has increased over the past year. That highlights an incipient trend. While the correlation between economic performance and support for democracy remains high, it is diminishing, says Marta Lagos, Latinobarometro's director.





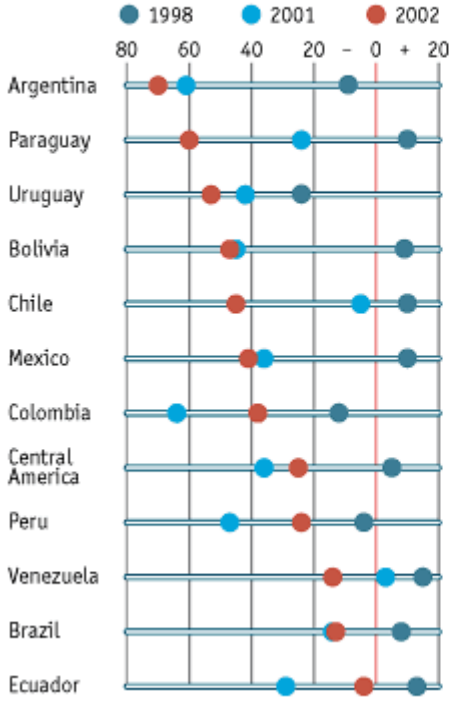
That makes it less likely that economic stress might result in a return to military rule. Contrary to outside perception, past military governments often enjoyed majority public support, at least at the outset. Such a regression could happen in countries where support for authoritarianism remains high, such as Paraguay. But it is unlikely in countries such as Argentina and Venezuela, which face political crises but where respondents put a high value on civil liberties, Mrs Lagos says.

The poll highlights the many problems of Latin American democracy. One is the generalised contempt for political parties (chart 7). Another is the perception of corruption; across the region, some eight out of ten respondents believe this to have increased in the past three years.

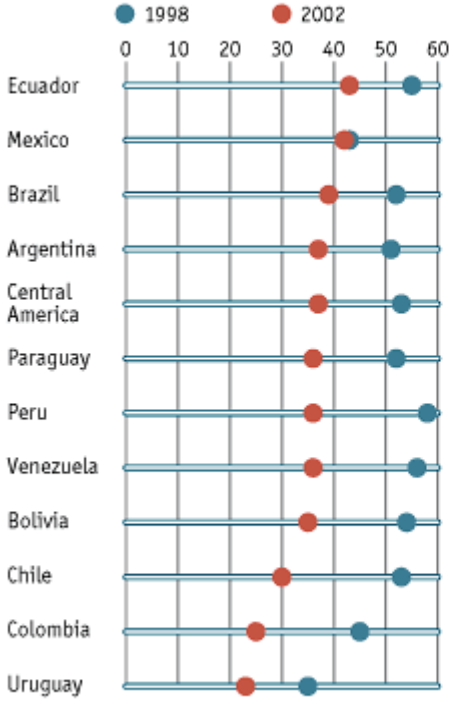
Latin Americans are also unhappy with some recent economic reforms. Most are now hostile to privatisation (see chart 5: charts 5-8 are in the last illustration below). And everywhere fewer (though still most) now think that the state should leave the economy wholly to the private sector (chart 6). Yet this appears to stem mainly from specific discontents about the way that public services have been privatised. Everywhere except Uruguay a majority of respondents still believe that “the market economy is best for the country”.

Private fears...

The privatisation of state companies has been beneficial, net, %* 5



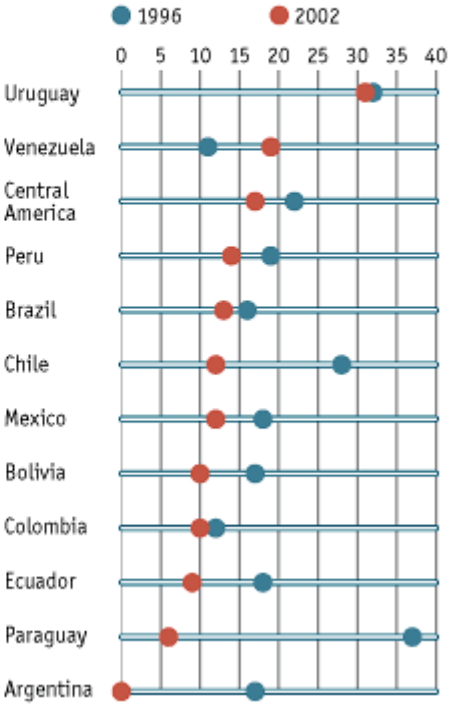
Those who strongly agree or agree that the state should leave economic activity to the private sector, % 6



...and party poopers

How much confidence do you have in political parties? 7

% responding "a lot" and "some"

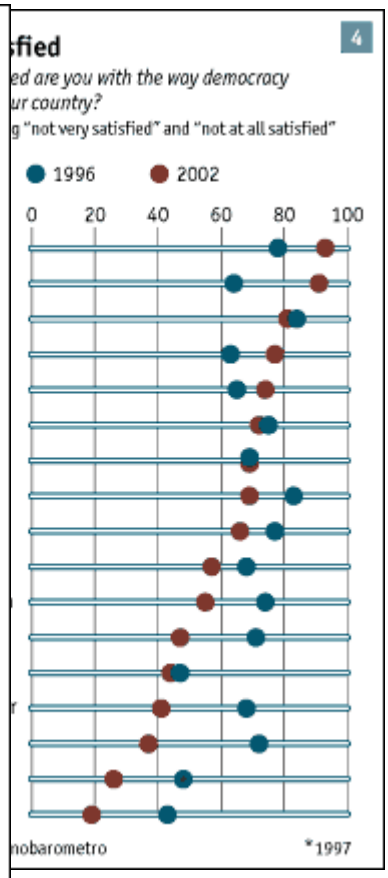


Where would you place yourself politically on a scale where 0 is left and 10 is right? 8

	1996	2002
Countries that moved to the left		
Argentina	5.7	5.2
Peru	5.6	5.3
Countries that have not changed†		
Bolivia	5.1	5.0
Brazil	5.1	5.3
Mexico	4.6	4.8
Uruguay	5.2	5.2
Countries that have moved to the right		
Chile	4.8	5.1
Colombia	5.7	6.9
Costa Rica	6.0	7.3
Ecuador	5.3	5.6
El Salvador	5.4	6.7
Guatemala	4.8	6.3
Honduras	7.1	7.8
Nicaragua	5.3	6.3
Panama	4.0	5.2
Paraguay	5.0	5.8
Venezuela	5.9	6.2

*"Strongly agree" and "agree" minus "disagree" and "strongly disagree" †By 0.3 percentage points or more

Source: Latinobarometro



Latinobarometro finds that only in Argentina and Peru have respondents moved somewhat to the left (chart 8). Not coincidentally, in both countries "neoliberal" reforms were carried out by high-handed presidents who have been accused of corruption. Across the region, most respondents defined themselves as being on the centre-right.

The poll finds that Latin Americans have a broadly favourable view of the United States, but that most opposed the American attack on Afghanistan. Interestingly, in Panama, itself invaded by America in 1989, a majority were in favour. But 80% of Argentine respondents and 74% of those in Mexico were against.

Latinobarometro is a non-profit organisation based in Santiago, Chile, which has carried out regular surveys of opinions, attitudes and values in Latin America since 1995. The poll was taken by local opinion-research companies in 17 Latin American countries, and involved 18,563 interviews in April and May 2002. The margin of error varied from 2.8% to 5%. Central America in the charts refers to an unweighted average of polls taken in Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua and Panama. The complete data from the survey are available for purchase. Further details can be found at www.latinobarometro.org

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Colombia's conflicts

State of commotion

Aug 15th 2002 | BOGOTA
From The Economist print edition

A crackdown against terror

Get article background

WHEN the guerrillas of the Revolutionary Armed Forces of Colombia (FARC) fired a dozen or so mortars at the presidential palace during the inauguration of Alvaro Uribe as the country's president on August 7th, they doubtless intended to provoke a reaction. It has come swiftly. Five days later, Mr Uribe declared a state of “internal commotion”, a constitutional provision which allows the government to decree a range of security measures, bypassing normal legislative procedures. “To counter terrorists who want to bring the nation to its knees, we are going to respond with all the means at our disposal,” said Fernando Londoño, the interior minister.

This device has been used only five times under Colombia's 1991 constitution, but never in a president's first week in office, nor with so much popular support. Most Colombians fear and condemn the FARC, whose 18,000-strong army is financed by kidnapping, extortion and drugs. The mortar attack, which security sources said used techniques passed on by the Irish Republican Army, failed to disrupt the inauguration, but killed 19 people in a nearby slum. In the past few months, the FARC has issued death threats against almost every elected official in the country, and staged sabotage attacks against bridges and electricity pylons.

The government's first use of its new emergency powers was to decree a wealth tax, to be paid by the richest 300,000 Colombians and some 120,000 companies. This should raise around $800m. That is enough for the defence ministry to equip and train at least 5,000 extra soldiers, 10,000 police, and—a second emergency measure—a new force of 100,000 part-time auxiliary police and soldiers, some of whom may be armed.

Mr Londoño said that more steps will follow. These will include measures to intercept and trace mobile-phone calls (but only on the orders of a judge), as well as stronger powers of search and arrest and curbs on freedom of movement. The government also wants to crack down on the finances of the FARC and other armed groups, by using the state of emergency to introduce new measures to confiscate assets derived from drug-trafficking.

The emergency powers last 90 days, but can be twice renewed. On paper, they are less draconian than the “state of siege” in force for decades before 1991. The government would like to go further. It will try to make many of the emergency measures permanent, via constitutional reforms.

But Mr Uribe will face several obstacles. One is Colombia's constitutional court, which must approve the emergency decrees. The court exasperated Mr Uribe's predecessor, Andres Pastrana, by revoking some of his measures, including an anti-terrorist law approved by Congress. The court's make-up has since changed. Mr Londoño, one of the country's most skilful lawyers, will try to cajole the court. He has already issued a veiled threat that he believes the judges “will reach the appropriate conclusions”.

Public opposition to the measures is so far largely restricted to trade-union leaders and human-rights groups but could grow. Mr Londoño insists that media and political freedom will not be curtailed, and that the government is “obsessive” about respecting human rights.

Given the new president's wholehearted backing, the onus now lies with the armed forces to start providing improved security. Mr Uribe has promoted General Jorge Enrique Mora, the army commander, to head the armed forces. He is respected within the army, but lacks political skills. The new president is trying to tackle other security weaknesses. He plans a joint intelligence service; the military and police

intelligence outfits rarely co-operate. Breaking with recent precedent, Mr Uribe has also named retired army generals to head both the corruption-riddled prison service and an office charged with confiscating drug traffickers' assets.

Mr Uribe's first measures also send a political message. The United States has provided Colombia with some $1.7 billion of mainly military aid in the past two years. But American congressmen have been pushing Colombians, especially richer ones, to pay more of the bill for their own security. The new measures were calculated to impress an American delegation which visited Bogota this week, prior to finalising an aid proposal for 2003.

The FARC will doubtless now throw what they can at Mr Uribe. A further upsurge in violence is likely. Turning the tide in Colombia's conflicts could take years. But Mr Uribe has already shown that he intends to try.

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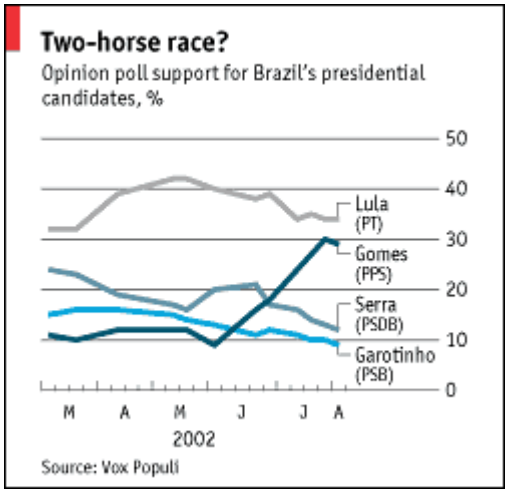
Politics in Brazil

Que sera, Serra

Aug 15th 2002 | SAO PAULO
From The Economist print edition

Is the government's—and the markets'—candidate doomed?

Get article background



UNTIL two months ago, it seemed likely that October's presidential election in Brazil would be won by Jose Serra, ally and close friend of President Fernando Henrique Cardoso. Since then, each new poll has brought Mr Serra bad news (see chart). Though support for the front-runner, Luiz Inacio Lula da Silva of the left-wing Workers' Party, has gently declined, that for Ciro Gomes, a renegade from Mr Cardoso's Social Democracy Party, has surged. Three polls this week brought a crumb of comfort for Mr Serra: both his fall and Mr Gomes's rise appear to have stopped. But it may be too late: some of Mr Serra's allies have deserted, and there is even talk of him quitting.

What has gone wrong? Perhaps Mr Serra, a good former health minister but poor stump campaigner, is simply the wrong candidate. Mr Cardoso might have done better to anoint Tasso Jereissati, another leading Social Democrat, who enjoyed broader support among the president's coalition partners. Spurned, Mr Jereissati threw his support behind Mr Gomes, his former protégé. Mr Serra also lost (to Mr Gomes) the backing of much of the conservative Liberal Front party, one of the pillars of Mr Cardoso's coalition and powerful in Brazil's north-east.

Secondly, Mr Serra has argued that only he can prevent Brazil following Argentina into financial chaos. Yet as turmoil has engulfed Brazil too (see article), that ploy has backfired. Ricardo Guedes of Sensus, a polling organisation, says that focus groups suggest that voters identify Mr Serra with a government which they blame for the country's vulnerable finances. Mr Serra's dithering over whether to pose as a candidate of change, when he stands for continuity, has not helped.

Mr Gomes has everything Mr Serra lacks: charisma, television skills, and an attractive partner in Patricia Pilar, a television soap star who is recovering from cancer. And he is untroubled by ideological consistency. As his ratings have soared, the whiff of power has bound together his improbable alliance of right-wing backwoodsmen and unreconstructed leftists. Mr Serra's attacks on his inconsistency and occasional fibbing have not so far dented his support, nor have corruption allegations against some of his aides.

Some of Mr Serra's allies, such as Cesar Maia, Rio de Janeiro's mayor, have put out feelers to Mr Gomes. If the likes of Mr Maia jump ship, that might finish Mr Serra. But he still has two hopes. Many voters have yet to make up their minds. And since he has the largest alliance (despite desertions), he will get the lion's share of the free television slots that candidates will enjoy from August 20th. If he uses these well, and if Mr Gomes's constant self-contradictions and frequent bust-ups with reporters start to drag him down, then Mr Serra might just make it to take on Mr da Silva, who lost the last three elections, in a run-off. But his chances hang by a thread.

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Politics in Venezuela

Chavez and the judges

Aug 15th 2002 | CARACAS
From The Economist print edition

The Supreme Court discovers its independence

Reuters

Uneasy on the throne

WHEN is a coup not a coup? Did the events of last April, when Venezuela's president, Hugo Chavez, was ousted by his own armed forces—only to be restored to power three days later—amount to a military rebellion, and thus warrant court-martials for the officers concerned? A narrow majority of the country's 20 Supreme Court judges think not. And that may have wider implications for Mr Chavez's grip on power.

In three successive votes in the past month, the latest on August 14th, the court has dismissed a preliminary case brought by the public prosecutor against four senior officers, arousing the ire of Mr Chavez and of his supporters. After each verdict, small but violent demonstrations have turned the centre of Caracas, the capital, into a no-go area. The city's police, controlled by the mayor, Alfredo Peña, who is an opponent of the president, have been fired on by demonstrators, and have begun firing back.

The court was previously known for its loyalty to Mr Chavez. Its verdict on the coup is only one of several signs of its increasing independence.
Cynics note that this coincides with a parting of the ways between Mr Chavez and Luis Miquilena, his former interior minister. Mr Miquilena, an octogenarian former communist, was the president's political mentor and the chief author of his “peaceful revolution” and Venezuela's new constitution. He was also instrumental in packing the court with loyalists, as he also did with other supposedly independent branches of government, such as that of the auditor-general and the ombudsman. Some of the judges now appear to have followed Mr Miquilena into opposition.

If that is so, is Mr Chavez still prepared to abide by the court's rulings? On the eve of the latest judgment, Mr Chavez warned the court that “the people” and the armed forces would not tolerate the acquittal of the rebel officers. “Some judges are manipulated by people who have a lot of money,” he declared on his rambling weekly radio and television show, “Hello President”. But as so often with Mr Chavez, he later seemed to tone down these incendiary comments.

But Mr Chavez's supporters are clearly rattled by the court. Rafael Vargas, the minister of the presidency, says that its decision to acquit the alleged coup plotters “could set the country on fire”. The real danger, he admits, is that this new judicial majority could back opposition moves to put the president himself on trial, for anything from human-rights violations to misuse of government funds. “The country is ungovernable without Chavez. Let's not forget that Venezuela has experience of both urban and rural guerrilla warfare,” Mr Vargas, who is himself a former guerrilla, says ominously. “And those oil wells, the source of the country's wealth, could be blown up in a minute,” he added.

Other advisers to the president have suggested that the court's decision over the coup could be revoked by referendum, or even by convening a new constituent assembly to eject the court. This is constitutionally dubious. Anyway, in 1999 and 2000, when Mr Chavez called and won six national votes, he still enjoyed overwhelming popular support. Recent polls suggest this has fallen to 30-35%, so he cannot be confident of winning a referendum.

Opposition leaders claim that the government is searching for a pretext to introduce a state of emergency, suspending some constitutional guarantees. But were it to do so, there is no guarantee that Mr Chavez's now-slender majority in the National Assembly would survive such a move, or that the

armed forces would tolerate it. So the time may indeed be approaching when Mr Chavez finds himself summoned to appear before his own formerly obedient court.

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The Koreas

A ray or two of light in the gloom

Aug 15th 2002 | SEOUL
From The Economist print edition

AP

But change in North Korea is coming too late to save the reputation of South Korea's president, Kim Dae-jung

FORTUNE no longer seems to favour South Korea's president, Kim Dae-jung. Hailed as a saviour when he took office in 1998, as the country teetered on the edge of bankruptcy, he has been brought low by corruption scandals that have landed two of his sons in jail and, after some disastrous by-elections, helped hand the opposition a majority in parliament just ahead of December's presidential election. Mr Kim is not eligible to stand in that election, but his party's nominee, Roh Moo-hyun, is now trailing badly in the polls. The party the president founded is expected to break up imminently; Mr Kim has already resigned from it in the hope that he will not drag it down further. Poor health kept Mr Kim, 76, from delivering his Independence Day speech this week. But in truth he probably feels he has little to celebrate.

Ultimately though, Mr Kim's legacy, for good or ill, is his “sunshine policy” towards North Korea, for which he received the Nobel peace prize after the first ever North-South summit, in North Korea, two years ago. For many months now, that policy has seemed to have run into the sand: partly because of the tough words emanating from Washington but mostly because the North seemed incapable of following up on its agreements with the South. Suddenly, after months of foot-dragging by the North, and a naval clash in June that left five South Koreans dead, “engagement”, as Mr Kim's policy is now named, resumed this week with ministerial talks about talks. Will these lead to real progress, or just another round of frustration? The answer will shape the verdict on the presidency of South Korea's brave but tarnished dissident-turned-leader.

This week's talks went well, up to a point. The two sides agreed to hold six more meetings in the next three months, including one to discuss a stalled project to reconnect road and rail links between the two countries. There will be more family reunions, and hundreds of Northerners will visit the South for the Busan Asian Games next month, where the (normally banned) North Korean flag will fly. The trouble is that little of this is set in stone: the North frequently cancels meetings at short notice. More frustratingly, no firm date was set this week for military-to-military talks, essential if work on the rail and freight links is to restart.

Still, if economic dialogue resumes as planned later this month, there could be more than the usual North Korean demand for goodies (the 300,000 tonnes of surplus rice South Korea was talking about sending northwards before the recent naval clash, for starters) on the agenda. Something in the last redoubt of

Stalinism is plainly stirring. Last month North Korea embarked on its first big economic changes in decades. Promises of cradle-to-grave provision by the state, which have left North Koreans struggling against poverty and starvation, have been abandoned: rationing of basic goods is to go; wages and prices are being increased, sometimes several-hundred-fold; the official value of the won has just dropped from 46 cents to just two-thirds of a cent, close to its black-market rate of half a cent.

Such reforms can have only limited impact at best, though. North Korea cannot tap the likes of the World Bank and the Asian Development Bank to rebuild its decrepit infrastructure until it achieves better relations, not just with South Korea, but also with Japan and the United States.

Talks with Japan resume next week. North Korea wants upwards of $10 billion in compensation for Japan's past colonial rule. Japan wants North Korea to account for more than a dozen Japanese citizens that it says have been abducted over the years by North Korean agents—an issue that has scuppered talks twice before.

But it is relations with America that will determine whether the hermit kingdom is truly bent on joining the world. The North has been sulking ever since the Bush administration pulled back from a deal on missile sales being negotiated by the Clinton team and named North Korea as part of the “axis of evil” for its proliferation activities. High-level talks had been due to resume in June, but were torpedoed by that month's naval clash with South Korea. The North has since expressed “regret” for the incident and James Kelly, a senior State Department official, may visit next month.

These talks will be tough. America wants a comprehensive dialogue covering not only missiles, but also ways to reduce the threat from North Korea's conventional forces, and checks that the North is keeping to a 1994 deal that shut down its plutonium production in return for two new reactors and interim deliveries of oil. North Korea's past bad behaviour has put the deal behind schedule, and this week it again threatened it would walk away from it unless America compensated it for electricity lost to past delays.

Veteran North Korea-watchers are not too disheartened yet. The North tends to step up the bluster when preparing to deal. Encouragingly, it says that four former Japanese terrorists will soon leave the country. Ousting them is one of the few steps North Korea still has to take to get itself off America's list of states that sponsor terrorism, which in turn would qualify it for possible World Bank help. Much could go wrong, and probably will, but the southern Mr Kim's hopes for a better future are not entirely dead.

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Indonesia

Back to barracks

Aug 15th 2002 | JAKARTA
From The Economist print edition

An end to reserved seats for the armed forces. Next, direct presidential elections

THE laborious process of overhauling Indonesia's semi-democratic constitution finally appears to be getting somewhere. In the early hours of August 11th, the country's supreme body, the People's Consultative Assembly (MPR), approved the fourth package of constitutional amendments since former President Suharto fell in 1998. Due to take effect in time for elections in 2004, the changes are by far the most sweeping yet.

The most decisive break from the days of Mr Suharto, when the army thoroughly dominated Indonesian politics, is the final elimination of the practice of reserving seats for the armed forces in parliament—supposedly in recognition of the their *dwi fungsi*, or “dual role”, as both political and military guardians. Their allocation has been progressively whittled down, but still stands at a useful 38 seats. These are now to go. In return, soldiers will be able to vote.

The MPR also considered, but rejected, the imposition of *sharia* for Muslims. Although Indonesia's Islamic parties promised that they will seek to revive the issue, possibly as soon as when the MPR meets next year, they look a long way from ever getting the two-thirds majority they need to push through such a change.

Indonesia's political architecture will change significantly under the reforms. The principles had already been written into the constitution in amendments at last year's MPR session, but the latest package makes much clearer how they will work in practice.

The MPR remains the supreme institution, as Indonesia's founding fathers decreed in 1945. However, the constitutional structure has been revamped to create a proper two-chamber legislature. The DPR, or House of Representatives, used to be the single-chamber legislature that passed ordinary legislation. After 2004 there will be a second standing body, the DPD or Regional Representative Council, which will function like a senate. The DPR and DPD sitting together will form the MPR, with the power to amend the constitution. The regional representatives formerly only sat during MPR sessions; the MPR has until now been an expanded version of the lower house. The creation of the permanent DPD gives the regions a stronger voice at national level. One of the main criticisms of the original 1945 constitution was that it gave too much power to the central government and president.

The most significant change to the MPR itself is that it will no longer be able to elect the president. Instead, there will be a direct presidential election, in two rounds. This means that the president elected in 2004 will have a much stronger popular mandate than any previous one. For the first time presidential hopefuls will have to campaign, work on their ratings and even participate in televised debate. That is a far cry from the old system, which relied on backroom deals among a small number of party bosses. Unsurprisingly, the party of President Megawati Sukarnoputri, who is not noted for her communication skills, opposed the direct election of the president, but in the end gave way.

So far so good. But if the political bills implementing these changes go through as drafted, the 2004 legislative election will retain some of the oddities of the Suharto system. These strongly favour the “big five” parties. New parties face almost insurmountable obstacles to qualify, although two large splinter groups from the existing big five might just make it.

Also, the system remains one of proportional representation rather than being constituency-based. Voters will still vote for a party rather than a candidate, although they will at least be able to specify which candidate from that party they favour. Critics believe these provisions still leave too much power in the hands of party bosses, and ample room for more political horsetrading and corruption.

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Pakistan

An empty election

Aug 15th 2002 | LAHORE
From The Economist print edition

Three popular leaders face arrest if they dare to return

Get article background

Reuters

Should I stay or should I go?

"I MISS Pakistan," says Benazir Bhutto. "I want to return to my country." That is easier said than done. Twice elected as prime minister of Pakistan and twice deposed, accused of corruption, Miss Bhutto languishes in self-imposed exile in London. Should she return to her country to lead her Pakistan People's Party (PPP) in the general election promised for October 10th, the country's current military dictator, General Pervez Musharraf, says she will be arrested. Miss Bhutto's husband, Asif Zardari, has spent the past five years in jail, facing charges of corruption and murder that he denies.

Another twice elected and twice deposed prime minister, Nawaz Sharif, is in exile in Saudi Arabia. He and his family were allowed to leave after General Musharraf overthrew him. Like Miss Bhutto, he faces arrest should he return. A third popular leader, Altaf Hussain, is also in exile. Mr Hussain heads the Muttahida Qaumi Movement (MQM), which represents the mohajirs (refugees) who came to Pakistan from India after partition in 1947. Mr Hussain fled to London in 1992 after the army cracked down on MQM-backed terrorism in Karachi.

As well as deterring these three popular leaders from returning for the election, the government has sought to ban their parties. It decreed that no party could contest the election if any of its office holders had been convicted of any offence. Mr Hussain was convicted in his absence of murder. Mr Sharif was convicted of terrorism shortly before he went into exile. Miss Bhutto was convicted last year by a special "accountability court" for "disrupting court proceedings" by not attending.

The party leaders have done their best to get round the decree. Mr Sharif has passed the presidency of his party to his younger brother. Miss Bhutto has announced the formation of the PPPP (the fourth P standing for parliamentarians), which plans to contest the election under her lieutenant, Makhdoom Amin Fahim. Mr Hussain long ago stepped down as chairman of the MQM, preferring instead the honorary title of *quaid*, or great leader.

The government has banned public rallies in the run-up to the election. The air is thick with stories of plans to rig the polls. The government is said to be bribing a number of small parties to combine under the banner of a pro-Musharraf "grand national alliance". Visiting officials from the European Union have been swamped by complaints that the government is fixing things to its advantage. They have said that the EU could halt its development aid to Pakistan if the elections are found to be rigged. Now Pakistan's foreign minister has taken offence and is refusing to meet the group, while the information minister has accused the EU of "interfering in the internal affairs" of Pakistan.

Miss Bhutto and Mr Sharif are still threatening to return to Pakistan at the last minute to whip their supporters into action by embracing the martyrdom of imprisonment. If General Musharraf is nervous, there is good reason for it. A tainted election will rob him of the legitimacy he craves and plunge the country into another round of instability.

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Thailand

Beware of the watchdog

Aug 15th 2002 | BANGKOK
From The Economist print edition

Its anti-corruption commission is Thailand's most trusted political body

MORE than a year and a half after Thailand's parliamentary election, the citizens of Ubon Ratchathani are keen to learn who won the race for the province's 10th district. Since the original poll, in January 2001, diligent voters have cast ballots in no fewer than three re-runs, and are scheduled to go to the polls again on September 8th. In theory, thanks to the sweeping powers vested in Thailand's Election Commission, the disqualifications and repeat polls could continue throughout the parliament's four-year term, until the commissioners are satisfied that no vote-buying, intimidation or any other form of fraud has influenced the result.

The Election Commission is just one of several new agencies brought into being by Thailand's five-year-old constitution. The drafters designed them to be powerful enough to extirpate the corruption that pervades Thai public life, and independent enough to work without interference from crooked politicians and officials. They are so powerful, in fact, that they have more or less superseded parliament as the focal point of Thai politics. Appointments to, and disputes between, the Election Commission, the National Counter-Corruption Commission (NCCC) and the Administrative and Constitutional Courts command far more attention than mere parliamentary debates. Politicians, belatedly grasping the new institutions' importance, are fighting to gain influence over them—with hearteningly little success.

Take the most celebrated case involving the new agencies: that of the asset declaration made by Thaksin Shinawatra, Thailand's prime minister, while serving as a minister in a previous government. The NCCC, which reviews all such declarations, found he had concealed some shares by registering them in the name of his driver, his maid and a security guard—a ruling that should have barred him from politics. But the Constitutional Court overturned the decision, by eight votes to seven, letting Mr Thaksin stay in office.

The drama might have ended there, had not the speaker of the Senate (another new institution) then asked the NCCC to investigate four of the judges who had voted to acquit Mr Thaksin. They had, after all, earlier convicted another politician under very similar circumstances. Although this convoluted sequence of events will not lead to a formal review of Mr Thaksin's case, it is already casting embarrassing doubt on the merit of his acquittal. Whatever its outcome, the saga has highlighted the huge potential for political point-scoring that the new agencies present.

No wonder, then, that politicians are trying to take advantage. Since the government commands an overwhelming majority in parliament, the opposition seems to think it is better off pursuing its grievances at the NCCC than in the chamber. Earlier this year, it petitioned the agency to investigate eight ministers for abuse of office. The parliamentary censure motions it launched at the same time were quickly squashed by the government majority—but the NCCC investigations continue.

Reformists fear that the government might use its majority to amend the constitution and emasculate the new institutions. But the odds of that seem to be receding. Different factions within the government want different changes, and may not be able to agree. Besides, public opinion is against it. Under pressure from the great and the good, both the government and the opposition have agreed to introduce amendments only for the sake of clarification, and not to reduce the watchdogs' clout. The NCCC, a recent poll found, is Thailand's most trusted government body. Clipping its wings would only drive parliament further down the ratings.

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China's mines

Pits of death

Aug 15th 2002
From The Economist print edition

Counting the cost of coal

Reuters

THIS week, 11 miners were reported to have died in an explosion in Lixin coalmine in China's north-eastern Heilongjiang province. At least 115 workers were killed at a mine in the same province in June, and 39 died in a mine in the nearby province of Jilin in July. China's vast mining industry suffers routinely from such appalling disasters, many of them attributed to safety standards that would not pass muster in a more open country.

Officially, more than 3,500 workers have been killed in mining accidents so far this year; the true death toll is thought to be much higher. Many disasters go unreported, sometimes with terrible consequences. In May, 21 miners were trapped underground after an explosion. The mine's owner tried to suppress news of the accident. By the time it leaked out, all those imprisoned were dead.

Many mines in China are privately owned. Some, like the one at Lixin, have been operating illegally. In response to growing public concern, even state-run newspapers have started to publish reports on the lack of safety in private mines. In a report last week on yet another mine fire, this one leaving 18 dead, the official news agency, Xinhua, noted that the mine lacked safety systems and that miners had been ordered to work secretly at night to avoid safety checks.

A Beijing-based diplomat notes that almost all the accidents reported in official newspapers take place at mines that are supposed to have been shut down. Often, these reopen as soon as inspectors leave: cash-strapped local authorities allow them to continue operating because they rely on the mines' tax revenues. The extent of poverty in rural areas means there are always people willing to risk their lives to earn a yuan.

State-run mines are claimed to be less of a problem. The government says it has invested more than $240m in safety equipment over the past year, and safety procedures have been improved in hundreds of mines. Another $700m is said to be on the way. But safety is only one of the government's worries about the industry. It is also concerned about air pollution, particularly in the run up to the 2008 Beijing Olympics, and is enforcing a switch from coal to natural gas in its big cities. Closing small mines is part of an effort to show that the country is cutting down on greenhouse-gas emissions and supports the aims of the Kyoto treaty.

Such gestures notwithstanding, coal remains king. China is its largest producer and consumer. Its mines employ millions of its people, and coal provides around 75% of its energy. With the demand for energy growing by about 3.5% a year and expected to double over the next 20 years, and despite strenuous efforts to provide other sources of energy, the International Energy Agency believes that coal will remain the country's dominant energy source for the foreseeable future.

China says that since 1997 the number of mines has fallen from 82,000 to 15,000. It plans to continue shutting down inefficient ones while improving those that are large, clean and safe. All laudable aims. But in the face of such strong demand, private, and sometimes illegal, mines will continue to supply the market for a long time—and no doubt claim more lives.

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India

In the beggars' court

Aug 15th 2002 | DELHI
From The Economist print edition

Where the conviction rate is 1%

A SCHOOL bus pulls into a leafy campus in north Delhi, stops before a squat brick building painted redder than brick red and discharges an unexpected cargo: a dozen men too woebegone and badly dressed to be scholars. They have been plucked off the street and may now be locked up for an indefinite period. Soon they will encounter one of Delhi's odder institutions: the beggars' court.

The oddest thing about the court is that it does not seem to have much to do with beggars. The bus's daily cull forms part of the enforcement of the 1959 Bombay Prevention of Begging Act, which Delhi has adopted. Technically, beggars are criminals, but their treatment is meant to be as much therapeutic as punitive. Delhi's Department of Social Welfare runs the bus, the remand centre and the institutions to which first-time offenders are sent for rehabilitation. That might be humane, if those caught in the roundups were actually beggars. “This act is criminalising poor people,” says Sunil Mow, a human-rights lawyer who helps them.

The men huddled outside the bungalow that serves as the court do not look like beggars. Only a few have the physical deformities of most who cadge coins at traffic lights in Delhi's richer quarters. One of the accused, Prakash, describes himself as a palm reader and astrologer. He says he was plucked off the street on his way to a client. Rakesh, who sells lime water in a market, was snatched away from his bicycle at a red light. “Is it a kidnapping?” he wondered.

These are the lucky ones, for they have scraped up enough money to be released on bail. Prakash paid 1,200 rupees (about $25), the better part of his monthly earnings of 1,500 rupees. Bail cost Rakesh 3,000 rupees. Where the money goes is a mystery. The court says it takes no money for bail. But the lawyers, who collect the money from their clients, insist that they keep just 300 rupees as their fee. The other accused languish in detention until the magistrate, Suraj Bhan, hears their cases, which should happen within a fortnight but often does not.

Mr Bhan presides impatiently over his tiny fan-cooled courtroom. Some judicial niceties are observed: there are a few legal tomes, but the magistrate says he cannot produce a copy of the statute he interprets. Before his entrance, the city's legal-aid lawyer fixes an old-fashioned courtroom collar to a soiled blue shirt. Mr Bhan rattles out verdicts: acquittal for a fruit vendor who slept rough, the same for a government functionary, who spends barely a second before the bar. A blind man's case warrants further investigation. Mr Bhan guesses the conviction rate in his court is 1%.

What about the other 99%? Ask the social welfare department, says Mr Bhan. K. Burman, a department official, insists that people are not picked up at random but admits that the 1959 act, which includes in its definition of begging “wandering about” the way a beggar would, gives “wide powers.” Perhaps the law needs a “fresh look,” he says.

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Plunder in Zimbabwe

The great terrain robbery

Aug 15th 2002 | CONCESSION, ZIMBABWE
From The Economist print edition

Reuters

Whites are not the only victims, and land is not the only asset being grabbed

Get article background

COLIN SHAND is a typical white Zimbabwean farmer. He's 58, tanned, rugged and jocular. He wears short beige shorts, and he keeps two hunting rifles, a shotgun and a shiny chrome revolver in his gun cabinet. He is deeply politically incorrect: he openly admits that he would not want his daughter to marry a black man. But until recently, he provided jobs and homes for 100 black Zimbabweans, who in turn supported more than 200 dependants. Now, his land has been seized by a rather smaller number of "settlers", his workers have fled with their families, and Mr Shand has been ordered to leave his home. The deadline for his eviction passed last week, but he ignored it, locked his farmyard gate and hunkered down. He has not needed his Colt .45 since he fought against black liberation in the 1970s, but he fears he may need it again.

Robert Mugabe's war against white farmers is entering its final phase. For two years, the Zimbabwean president's supporters have staged "spontaneous" invasions of white-owned farmland, seizing plots, beating up farmworkers and enjoying total immunity from prosecution. Now, 95% of the country's 4,500 commercial farms have been earmarked for seizure without compensation. Like Mr Shand, most farmers were legally obliged to leave their homes last week. Some hoped that Mr Mugabe might relent a little in a televised speech he gave on August 12th, to commemorate the liberation war. But they were disappointed. "We brook no impediment," he said, "and we will certainly suffer no avoidable delays."

The president says he is simply reclaiming for poor blacks the land that was stolen from their ancestors. But the recipients have often been his far-from-poor cronies. He promises that the new farmers will be *in situ* in time for the new planting season in October. But beneficiaries of past takeovers, who rarely had much farming experience, have allowed irrigation systems to crumble and once-fertile fields to revert to barren bush. Cereal production has fallen by two-thirds over the past two years, partly because of drought, but mainly because the most productive farmers, who have traditionally prevented drought from turning to famine, are hiding by their gun cabinets. Half of Zimbabwe's 12m people need food aid, according to the World Food Programme.

Justice for Agriculture, a pressure group, estimates that 60% of farmers are defying their eviction notices. The *Herald*, a government mouthpiece, says that most have left. No one really knows. It is unlikely, given shortages of fuel and competence, that the government could evict all the farmers in a

swift and orderly fashion. But they could easily murder a few to encourage the rest to flee. Since 2000, Mr Mugabe's heavies have killed 11 farmers and tortured thousands of farmworkers. Farmers fear they are poised for a final shove.

But Mr Mugabe's terror campaign costs money. The militia need to be paid, transported and kept supplied. The police and army need to be rewarded for their loyalty. Where will the old despot find the cash? His regime has never got by merely by levying taxes on income and the like. Aid used to keep it afloat, but this has now dried up, barring the odd handout from Libya's Muammar Qaddafi. So now Mr Mugabe is filching his subjects' savings, partly by printing money, and partly by more direct means.

The other grand grab

The chief of these means is a pensions-grab almost as daring as his land-grab. Private pension funds are obliged to “invest” 45% of their assets in treasury bills that pay 25% a year. Since inflation is 114%, this amounts to confiscation.

To recap: an illegitimate government is stealing its people's life savings to keep itself in power, so that it can continue implementing its ruinous policies. It is as if someone took out a mortgage on your house and used the cash to pay thugs to burn it down. Unless most of Mr Mugabe's policies are reversed, Zimbabwe will be left with no savings, and a dramatically reduced income. If the intention is to revert to a feudal society, where peasants scratch a mean subsistence and can be thrown off their land at the whim of their political overlords, Mr Mugabe is doing well.

Meanwhile, Mr Shand is feeling tired and nervous. Finally, the strain of listening for approaching footsteps grows too much, so he switches on television and watches a rugby match at full volume. “It's like waiting for a war to start,” he says.

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Iran, Iraq and America

Distrust, in all around

Aug 15th 2002 | TEHRAN
From The Economist print edition

The inescapable quandaries facing Iran's president

Get article background

IN RETURN for staying neutral in the 1991 Gulf war, Iran persuaded Saddam Hussein to surrender some disputed territory, and to start releasing the Iranian prisoners he had been holding since the two countries fought in the 1980s. More than a decade on, Iran's leaders are hoping to exploit Mr Hussein's renewed vulnerability. But neutrality may now be harder to maintain. Much as they hate the idea of American troops on their western border, helping George Bush in Iraq could be a last chance for the clerical regime to stay off the president's list of condemned countries.

Ayatollah Baqer al-Hakim, a Tehran-based Iraqi dissident with followers among Iraq's Shia majority, is deeply involved in the Iranian-Iraqi-American imbroglio. America now wants Mr Hakim's co-operation in generating a popular uprising in Iraq, but he and his small army need Iran's permission to do so.

The Americans are anxious to avoid a repeat of the fiasco after Mr Hussein's defeat in 1991: an American-incited rebellion among Iraqi Shias came to a tragically bloody end when Mr Hakim's men (and members of Iran's Revolutionary Guard) crossed the border, and an alarmed America withdrew its support for the venture. When Mr Hakim's brother returns later this week from talks with American officials and other Iraqi opposition leaders, he will no doubt tell the Iranians what America now expects of them.

Ever since Mr Bush included Iran in his “axis of evil”, America's pronouncements have been menacing, but vague. Earlier this month, Zalmay Khalilzad, one of Mr Bush's senior foreign-policy advisers, made it clear that America had despaired of Iran's “ineffective” reformist president, Muhammad Khatami. He did not, however, as some senators and congressmen would have liked, call for a new regime in Iran. What is more, Mr Khalilzad said that America was open to discussions with Iran, notably on creating an Iraq that was no longer a threat to its neighbours.

But Mr Khatami's distrust of Mr Bush has risen since the Americans, far from thanking Iran for its help in unseating the Taliban in Afghanistan, have been accusing the president's conservative opponents of helping al-Qaeda fighters to safety. On Tuesday, Donald Rumsfeld, the defence secretary, reacted to the “news” that Iran had handed over 16 suspected al-Qaeda fighters to Saudi Arabia by insisting that many more were still in Iran.

The Iranians responded by saying that they have over time arrested some 150 al-Qaeda suspects, nearly all of whom have already been handed over to various countries. The 16 Saudis were in fact repatriated in May. Hamid Karzai, the Afghan president, managed to sound equally friendly to Iran and to America, when Mr Khatami visited him in Kabul this week.

Iran's government looks for rewards in a post-Hussein regime, such as the liquidation of the Iraq-based People's Mujahedeen, which has spent the past two decades threatening it with bombs and bullets. But its ability to influence events in Iraq is hampered, not least by Arab fear of the effects that Iran-sponsored Shia chauvinism might have on their own Shia minorities. And Mr Khatami is in a quandary. Even if he co-operates with America, his conservative opponents could repeat the spoiling tactics they are said to have employed in Afghanistan.

For the moment, the Iranians are concentrating on short-term gains. Mr Hussein, fighting for his life, has quietly accelerated the repatriation of his remaining Iranian prisoners of war: fewer than 1,000 are thought to be still in Iraqi hands. Iraq is also keeping the Mujahedeen quiet. In return, Iran will continue

to turn a blind eye to the cross-border smuggling that keeps Iraqis supplied with food and other goods.

But Iran's co-operation has limits. At a recent meeting with Mr Hussein's elder son, Iranian military officials are said to have refused to hand over the 100 or so war planes that Iraq misguidedly entrusted to Iran during the Gulf war.

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Iran and Kurdistan

Looking both ways

Aug 15th 2002 | DARASHISH, NORTHERN IRAQ
From The Economist print edition

While punishing al-Qaeda elsewhere, Iran may be helping it in Kurdistan

Get article background

EVERY evening Kurdish *peshmergas* (guerrillas) trade mortar fire with Ansar al-Islam, a radical Islamic group, believed to have close links with al-Qaeda. According to *peshmerga* commanders, the group, which now has some 700 armed men, about one-tenth of them Arabs or Afghans, penned into a small enclave on the Iraq-Iran border, is getting substantial help from Iran.

Villagers coming from the area under Ansar's control say that Iran brings arms and ammunition to the frontier, and that these are then brought over on horseback. The *peshmergas* say that the Iranians have recently given the group truck-mounted Katyusha rocket-launchers, and helped them target their artillery from positions inside Iran.

Elsewhere Iran has been helping America in its fight with al-Qaeda. It denies that it has any relations with Ansar al-Islam. But if the charges are true, how can the contradiction be explained? Perhaps because the Iranians, fearful lest federal, let alone secessionist, ambitions infect their own 8m Kurds, do not want to see the emergence of a strong, stable Kurdistan as part of a future federal Iraq.

This part of northern Iraq is controlled by the Patriotic Union of Kurdistan (PUK), whose leaders have always had good relations with Iran.They are loth to accuse the Iranians directly, partly because they fear that Iran would then close its border to them. But *peshmerga* commanders argue that Ansar, sealed between PUK lines and the Iranian border, could not have got its weapons from anywhere else.

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AIDS in Uganda

Was the miracle faked?

Aug 15th 2002 | KAMPALA
From The Economist print edition

No, but possibly exaggerated

YOU can recognise Uganda's health ministry by the gleaming gold letters on the gate, the car park full of sports utility vehicles, and the fact that the lifts work. Erected two years ago with ample donor funds, it stands out from its nearest neighbours, a clutch of tin-roofed shacks. Foreigners love giving money to Uganda because it is that rare thing: an African success story. Specifically, the country has achieved a miraculous reduction in the level of AIDS infection. Or has it?

The official story, repeated often and with reverence at AIDS conferences, is that infection rates were stratospheric when Yoweri Museveni seized power in the 1980s. Unlike other African leaders, Mr Museveni did something about it. He spoke endlessly of the dangers, the radio waves were opened to frank talk about safe sex, shops were stocked with condoms, and so on. The epidemic was rolled back: earlier this year, the president said that his government had cut HIV prevalence from 30% in 1990 to 6.1% last year.

But an American medical researcher now questions the precision of this miracle. In an article in the *Lancet* last month, Justin Parkhurst, of the London School of Hygiene and Tropical Medicine, argues that it is based on flimsy evidence. Much of the data come from testing pregnant women seeking treatment at urban health clinics, which, he writes, is “hardly indicative of a nation where about 87% of the population live in rural areas.” Nationwide, he suggests, infection rates were never as high as 30%. The oft-cited dramatic drops in HIV prevalence were recorded only in a few places. Elsewhere, the decline was more modest. Mr Parkhurst concedes that Uganda has been uniquely successful in fighting AIDS. But he claims that its achievements were exaggerated, with normal standards of proof lowered in order “to provide the international community with the African success story it wants.”

The article sparked pandemonium in Uganda. Newspapers splashed Mr Parkhurst's findings on their front pages. The country's top health officials and AIDS researchers denounced the article as “slanderous”, and accused its 28-year-old author of being a publicity hound seeking a career-making controversy. But, privately, some outside AIDS experts say that Mr Parkhurst, however undiplomatically, may have hit on something. No one seriously disputes that infection rates have been falling in Uganda, but many doubt that they have dropped as precipitously as the authorities claim.

Why fake a miracle? Mr Parkhurst suggests that, just as Wall Street pressures corporations to report ever-increasing earnings, the behaviour of international donors encourages poor countries to accentuate the positive. If aid is not seen to work, the donors may move on. But accuracy matters: if other African countries with horrific AIDS epidemics are to learn from Uganda's genuine success, they need to have precise information about what the country managed to do, and how.

Meanwhile, inside the health ministry, a counter-attack is being hatched. *New Vision*, a state-owned paper, printed a lengthy rebuttal of Mr Parkhurst's claims, saying he ignored data from other centres, such as blood banks. The ministry was also able to announce more good news: according to the latest data, HIV prevalence in Uganda has now dropped to 5%.

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Israel and Palestine

Where causing pain is an end in itself

Aug 15th 2002 | JERUSALEM AND JENIN
From The Economist print edition

Two years of violence, two lousy strategies, and still no end in sight

Get article background

AP

After a suicide bomb

"IT TOOK the first *intifada* to push me off the fence and into the peace camp," says Edward Cohen, a soft-spoken venture-capitalist in Jerusalem. "It took the second *intifada* to push me back up and over to the other side of the fence." And so say many other Israelis. Next month the Palestinian uprising that broke out after the failure of Bill Clinton's peacemaking at Camp David in the summer of 2000 will enter its third year. It has not only claimed the lives of about 1,500 Palestinians and 550 Israelis. It has also destroyed the belief of many good people on both sides in even the possibility of peace.

The visitor to Israel finds a sad and frightened nation. Life goes on, but in the knowledge that any bus, café or university campus could be the target of the next suicide bomb; the guards posted outside shops and restaurants seem almost to flinch as they ask customers to open their bags. Mixed with the depression is a black feeling of betrayal—by the Europeans, for what Israelis consider a failure to denounce this terrorism; but above all by the Palestinians, for reneging on their promise under the Oslo peace accords to grasp the olive branch and put aside the gun.

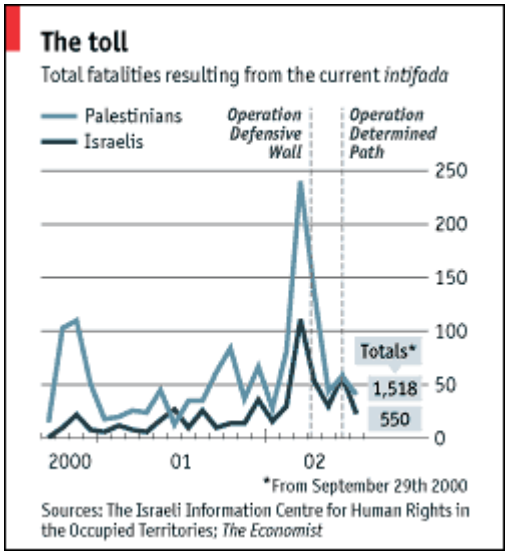
This latter betrayal is felt most keenly by those who worked with Yasser Arafat's Palestinian Authority (PA) to steer to peace by the Oslo road-map. Jacob Perry, now head of a telecoms firm, but until recently director of the Shin Bet security service, says it is now plain that the PA was never serious about clamping down on the hardline groups such as Hamas and Islamic Jihad. From 1993 onwards, he claims, the PA began to smuggle arms and ammunition into the West Bank and Gaza to prepare new violence. When the fighting started, Mr Arafat's own Fatah organisation, not the Islamists, conducted most attacks.

To Ariel Sharon and his Likud Party, the bitterness of those in the former Labour government of Ehud Barak, who put their faith in Mr Arafat and Oslo, merely shows what dupes they were. Today Labour clings on as a demoralised bit-player on the margins of Mr Sharon's coalition, claiming without conviction that by doing so it moderates his handling of the *intifada*. Fear of the voters is a more plausible motive: Ephraim Sneh, one Labour minister, says simply that with some 600 Israeli dead in a terrorist war, "our voters would punish us if we left the government now. They don't want the strategy to be left in the hands of the hardliners."

But what, exactly, is the strategy? Is Mr Sharon, as his critics say, merely flailing about for a military answer to a problem that cries out for a political solution?

He is not that simple. Though the military challenge dominates the thinking of his inner circle, none of his top advisers believes that all the bombers can be stopped by force alone. One admits that since the Palestinians no longer observe any red lines, "the sky's the limit" for their attacks. The army expects the Palestinians to turn soon from strikes that take a dozen or a score of lives at a time to "mega-terror" of the sort pioneered by Osama bin Laden. In the meantime, its aim is to minimise Israel's casualties. Mr Sharon's two big operations so far—the reconquest of the West

Bank under operation “Defensive Wall”, and bottling up its inhabitants under “Determined Path”—have indeed delivered short-lived lulls (see chart).



The Arafat fixation

Besides, Mr Sharon's diplomacy, fixated for months now on the removal of Mr Arafat, has arguably been more successful than his military moves. The speech in June in which George Bush surprised the world by calling for a new Palestinian leadership and reform of the PA is seen by the prime minister's men as a famous victory. Israel, they say, invented the idea of demanding the reform of the PA, and planted this notion methodically not only in the mind of the Americans but also in those of several European and Arab governments. Though they dare not say so, the Israelis aver, countries such as Egypt and Jordan accept that no political progress can be made while the PA is under the impossible Mr Arafat. Their quarrel is not about whether he should go, only how.

For the present, the policy of choice is gradual marginalisation. Israel wants countries that talk or give money to the PA to bypass Mr Arafat himself. As time passes, it is hoped, his lieutenants will check back less and less with their nominal president. The aim is to whittle away his authority and build up his rivals. Won't that merely deprive the Palestinians of their paramount leader, and Israel of a needed interlocutor? On the contrary, say Mr Sharon's men. Whoever takes his place will need the political and financial support of the rest of the world, and this in turn will require accepting what Israel says Mr Arafat refuses to see, “that terror is a currency that isn't traded any more.”

As to who this successor might be, Israel's thinking is a study in vagueness. The Israelis acknowledge that no other Palestinian commands the loyalty of all of Palestine's complex factions. Muhammad Dahlan, who heads Palestinian security in Gaza, has no following in the West Bank; Jibril Rajoub, his West Bank counterpart, whom Mr Arafat recently sacked, has none in Gaza. The Israeli hope is that a collective and more pragmatic leadership will arise. Only then, it is explained, can Mr Sharon show the generosity he refuses to show while the *intifada* still rages. In accordance with Mr Bush's plan, the Palestinians will be allowed to declare a “provisional” state, whose borders will remain undetermined until after a couple of years of quiet.

Oslo revisited

If this is a plan, it is a desperate one. It is, in effect, Oslo all over again, minus Mr Arafat, with the clock rewound so that the date for settling all the wicked issues—borders, settlements, refugees—is deferred even longer. After all their loss of life and livelihood, no new leadership could easily ask the Palestinians to give up their fight for so little. Even Mr Perry, the former secret policemen, concedes that the failure of Israeli governments to deliver enough political movement helped to provoke this *intifada*, and that some big gesture will be needed to end it. But—here is an infernal Catch 22—how can Israel appear to concede under fire without inviting more of it?

That is a question the Palestinians might profitably try to answer. For if it is hard to see how Israel intends to defeat the *intifada*, it is no less difficult to see how the Palestinians intend to win it.

In the beginning, Mr Arafat may have hoped to force international intervention, so producing a settlement more favourable than the one offered by Mr Barak. He has indeed wrung out of Mr Bush a clearer “vision” of Palestinian statehood than any previous Republican president has given. But America's

vision is for the long term, and Mr Bush has meanwhile allowed Mr Sharon to reconquer the West Bank.

If the Palestinians hoped that a new *intifada* would bring the doves to the fore in Israel, the opposite has happened. Israel's peaceniks—the “dupes” of Oslo—have been waning, and far-right voices, calling now for the “transfer” of all the Palestinians to neighbouring countries, have waxed in their stead. “They call me a racist,” says Benny Elon, one Israeli MP who cannot understand why so few see the beautiful logic of this policy. “But that is because my critics refuse to face reality.”

In private, some prominent Palestinians confide that they do not expect much good from this latest *intifada*. Comparing it unfavourably with the uprising of the late 1980s, some say it is not really an *intifada* at all. Last time, the Palestinians chose not to use firearms, putting their faith in a mass movement with clear political objectives. This one, they say, has been hijacked by the armed factions, bringing more harm to the Palestinians than to Israel.

AP

Routine in the West Bank

But such views are far from representative. Indeed, a terrible aspect of the uprising is that to many Palestinians its political objectives are secondary. In a mirror of Israel's mood, they too feel betrayed by the Oslo years. Having waited patiently for statehood, all they got was more Jewish settlement and, as they see it, an insulting offer from Mr Barak. Few think of the *intifada* as an instrument, soberly chosen to achieve a precise diplomatic end. Most insist that it was a reaction—the only available one—to injuries which the Israelis inflicted on them. As the rage of each side mounts, the infliction of pain on the other becomes strategy enough in itself.

Back to 1947

Who will prevail? In Jenin, a West Bank city girdled by Israeli armour and torpid under the summer sun, Muhammad, a portly civil engineer with nothing to build, sits beaming in his barren office and explains with perfect lucidity the beauty of the suicide bombings—rather as Mr Elon in Israel's parliament explained the beauty of “transfer”. Israel has its smart bombs, he says, but ours are smarter because they can think, see, and change direction. They have wrecked Israel's economy, scared off investment, discouraged more Jews from coming and persuaded many to leave. By striking fear into the Israeli heart, they have made the Jews feel that Palestine is not theirs: “You do not feel afraid if you are in your own country.”

Would Muhammad make peace if Israel returned to its pre-1967 borders, as the PA says it would? “Why the 1967 borders?” he asks. “Those Nazis took 78% of Palestine, leaving us only with the dry and barren 22%. Our aim is 100%.” He adds as an afterthought that if, and only if, the Palestinians felt “very generous” they might let a Jewish state exist in the borders marked out by the UN partition plan of 1947. This would have been a state of little enclaves, rather like the one the Palestinians now accuse Israel of trying to force on them. Trapped in the wretched symmetry of dual victimhood, the two nations battle bloodily on. It is hard not to conclude that the worst is yet to come.

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The Benes decrees

A spectre over Central Europe

Aug 15th 2002 | PRAGUE
From The Economist print edition

Even now, a quarrel over one obscure side-effect of the second world war could threaten the enlargement of the 21st-century European Union

HAS Central Europe come to terms with the second world war? When Tony Blair visited Prague on an arms-selling mission earlier this year, he was assailed by Czech journalists. But not for details of the fighter aircraft he was trying to flog: what they wanted to know was Britain's position on the Benes decrees.

The Benes what? Mr Blair looked at his notes, and flannelled. Well he might. The decrees, providing a legal basis for the eviction of ethnic Germans, the "Sudeten Germans", from Czechoslovakia, were issued by President Edvard Benes in 1945. Yet they are still a live political issue—and a growing one. They have been used by populist politicians across Central Europe. They figured in Hungary's elections in April and in the Czech ones in June. They will figure in the Slovak and the German elections next month. They could even threaten the enlargement of the European Union.

The world war was presaged by the Munich agreement of late 1938, when Czechoslovakia's fair-weather friends bought off Adolf Hitler by donating him swathes of its border-lands inhabited by the allegedly oppressed Sudeten Germans. War was guaranteed by his seizure of most of the rest in March 1939. Hungary too took slices of territory, Poland small bites. In 1945, the liberated Czechs were not much worried about the human rights of their ex-occupiers. The troops had gone; the civilians, men and women, ancients and infants, should go too.

Czechoslovakia, created only after the first world war, had been a diverse place. When Tomas Masaryk, its founding father, died in 1937, his coffin was shouldered by six soldiers, one for each of its nationalities: a Czech, a German, a Slovak, a Hungarian, a Ruthenian and a Pole. The country also had many Jews, classed as Czech, Slovak or German according to their language. But that was before the storm. The Jews were murdered by Hitler. First Hungary, then, after the war, the Soviet Union grabbed Ruthenia, in the east. The Poles went to Poland, many Hungarians, some under compulsion, to Hungary.

The biggest shift was the expulsion of the Germans, a quarter of the population in 1938.

Under the decrees, ethnic Germans were stripped of their citizenship and property, without compensation, and thrown out, unless they could prove that they had shown their loyalty to Czechoslovakia during the Nazi times. By normal standards, this was monstrous, and Austrian and German right-wingers, saying that the decrees have no place in modern Europe, want them annulled at once. And if today's Czech Republic won't do that, say some, it should not be let into the EU.

The Czechs won't. In part because annulling the decrees would open the floodgates to property claims from Germans. But mostly for patriotic reasons: Czechs—like the Poles, who, with the Red Army, ruthlessly expelled 6m-8m Germans from what, after the war, became western Poland—feel those who began an appalling war have no claim to revise its effects.

There is no denying the Sudeten Germans suffered terribly. Before or after the decrees, some 2.4m were expelled. Even Czech historians say some 19,000 died in the process, 6,000 violently. Sudeten German groups today—for they still exist in Germany and Austria, and they haven't forgotten—say far more died. It could be: just last month a Czech historian uncovered new evidence suggesting that the Benes government covered up mass executions of German civilians.

Even nationalist-minded Czechs now admit there were excesses in the wild days just after the liberation. Witnesses tell of lynchings: SS men burned alive or tethered to workhorses and torn limb from limb. Innocent Germans were randomly scalped or shot. Countless women were raped. Even the sick and elderly did not escape being beaten. A Hungarian going home via Prague in 1945 wrote that what he saw there made his stay in a Nazi concentration camp look “like a holiday”. Even in late 1945, when tempers had cooled and order had been restored, 50,000 people turned out in Prague to watch the execution of Germans as an entertainment.

Czechs shrug this off. It was sad, they say, but their country had suffered more than six years of often brutal occupation. The policy of expulsion, and the decrees that authorised it (also hitting some Hungarians in Slovakia, though they suffered less), were backed by the victorious Allies. They were confirmed by later bilateral treaties, including one between Czechoslovakia and West Germany. Germans are welcome back for visits; local councils are increasingly happy to tend German graves and to remember the German bit of their town's history. There are many positive stories of returnees. But there will be no apologies or return of property. “We're not getting down on our knees for them,” says an elderly farm worker on what were once ethnic-German fields near Litomerice (ex-Leitmeritz) in northern Bohemia.

Czech officials point out that 91% of Sudeten Germans voted for a pro-Nazi party in the 1938 elections. They welcomed Hitler's troops. They were his “fifth column”, “traitors”, according to Milos Zeman, who retired as Czech prime minister in June. The new man, Vladimir Spidla, is more diplomatic but just as firm: he will not bow to external pressure. Nor very well could he: in April, the then parliament voted by 169 to none to retain the Benes decrees and refuse to reopen issues arising from that period. The most the Sudeten Germans can hope for, say insiders, is a statement of regret and a few memorials.

The Sudeten influence

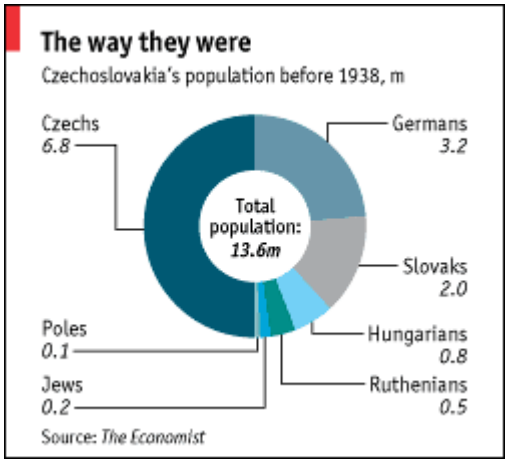
That might be enough for Germany. Its chancellor, Gerhard Schröder, is committed to a 1997 agreement with the Czechs which holds that bilateral relations should not be infected by history. But even he cancelled a visit to Prague this spring in protest against Mr Zeman's remarks. And what if the conservative challenger, Edmund Stoiber, wins September's election? He is Bavarian, his wife a Sudeten German who fled as a girl with her parents from western Bohemia. Sudeten Germans form an ageing but still influential part of his electorate. He is often at their gatherings with his wife, sometimes lingering over photo albums of long-Czechified villages and towns. Mr Stoiber has said that he is not willing to draw a line under the past.

In office, he might think otherwise. German companies are the main foreign investors in the Czech economy. Volkswagen has made a huge success of Skoda, a Czech car maker. The last thing it or other German firms want is to see historical grievances sour their business climate.

Austria is tougher on the issue. Curiously, you might think: it took in only a few of those expelled. But relations between Prague and Vienna are terrible. Some of the bad blood goes right back to

Austria's imperial rule of the Czechs. Some is bang up-to-date: a row over a Czech nuclear plant. But Austrians like to pretend that (except by birth) Hitler was nothing to do with them. And their chancellor, Wolfgang Schüssel, is the darling of the Sudeten German lobby. “Injustice never lapses,” he tells its members, to Czech annoyance.

Right-wing Austrians want no part in a dialogue set up by liberals from both countries to improve relations. Egged on by the governor of Carinthia, Jörg Haider, whose Freedom Party is Mr Schüssel's coalition partner, they threaten to do all they can to block Czech entry into the EU unless the issue of the Sudeten Germans is resolved.



The Polish question

Does all this matter? Can ancient wrongs really be allowed to meddle with the future of 21st-century Europe? Yes, for there is another ghost at this feast of ill-will.

The dispute over the Benes decrees has already cut into Czech enthusiasm for the EU. What alarms diplomats is that it could lead to a closer look at the Poles' expulsion of Germans. That is a taboo subject for the many Poles who still distrust and dislike the neighbours who invaded them in 1939, killed millions and for decades after 1945 claimed that parts of Poland were merely “under Polish administration”. Poland restricts sales of farmland to foreigners, and has negotiated with the EU a 12-year transition period for ceasing to do so. The aim was to reassure Poles in western Poland that the former German owners were not going to start buying back their land. But 12 years is not eternity, and support for joining the EU is already fragile in Poland, notably among farmers, albeit mainly for agricultural-policy reasons. Populists like the farmers' leader, Andrzej Lepper, would love to use history to win a no vote in next year's referendum on joining the EU.

That fear for Poland is why Günter Verheugen, who oversees enlargement for the EU, has gone out of his way to reassure edgy Slavs. The Benes decrees, he says, “will not create an obstacle for the accession of the Czech Republic into the EU”. The Czechs should respect Austrian sensitivities, he says, but “basically this is a political, not a legal problem”.

Well, so it is. And common sense says that if far greater and more recent quarrels could be put aside to create what is now the EU, so can and should this one. But not even international politics is conducted by smooth, sensible diplomats or Eurocrats, removed from popular feelings. The Benes decrees are ancient history, but they revive it too. Super-patriots in the EU's Germanic members could usefully note that respect for sensitivities is a two-way game.

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Floods hit Central Europe

Aug 15th 2002
From The Economist print edition

AP

Nature knows no citizenships or frontiers. This week parts of southern Germany, Austria and the Czech Republic alike were ravaged by rivers swollen by torrential rains. The Elbe swamped areas of Dresden; Salzburg was cut off; the mediaeval centre of Prague (above) was saved, just, by emergency flood barriers, but huge numbers of people in the city had to flee their homes, as the Vltava river rose to levels unreached since 1890. In these three countries 25 people died. Russia was still harder hit: as flash floods last weekend swept roads and cars into the Black Sea, some 60 people perished.

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Germany's election

Schröder still has a chance

Aug 15th 2002 | BERLIN
From The Economist print edition

His Social Democrats are way down in the polls, but not yet out

Reuters

Schröder's hopes rest on Hartz

JUST five weeks short of the election, the outlook for Gerhard Schröder is grim. Instead of picking up, the economy is again in deep trouble. The number of jobless is almost back to where it was when Mr Schröder came to office in 1998, and rising. Bankruptcies are soaring, share prices in the basement. Freak floods are threatening lives, homes and crops. And the government, lurching from one crisis to another, has no answer to any of them. No wonder opinion polls show the ruling Social Democrats trailing their conservative rivals by 6-8 points, as against 2-4 in June.

So is the game up for Mr Schröder? Most pundits think so. Yet one voter in three is still undecided, and he still holds a couple of potential trumps.

First, for all his government's woes, he himself remains far more popular than his challenger, Edmund Stoiber. The Bavarian leader scores higher on jobs and the economy, the two main campaign issues. But Mr Schröder is widely seen as the better leader, especially in a time of crisis. Their manifestos suggest little to choose between the two men. Both say they want to boost the economy, create jobs, secure pensions, improve education, help families and pump new aid into the ex-communist east. Both talk of slashing taxes, welfare contributions, government spending and public debt. Neither explains how this twofold miracle will be achieved.

Secondly, Mr Schröder has the bold and potentially far-reaching labour-market reforms put forward by a government-appointed commission chaired by Peter Hartz, Volkswagen's personnel manager. Its report, already widely leaked, was due out officially on August 16th. Mr Schröder still has time, just, to make use of it.

So the commission's proposals, already broadly backed by employers and trade unions alike, will be put before a special Social Democratic conference this weekend. The cabinet will announce its first measures, ones not requiring legislation, next week, and send further ones to the Bundestag as a bill during the debate on the 2003 budget early next month.

The commission thinks Germany's 4m jobless could be halved within three years were its recommendations implemented promptly. The key proposal is for the creation of state-run agencies, alongside the present unemployment offices, which would take on those still unemployed after six months without a job, and hire them out to employers. Any who refused would have their unemployment benefits cut. All the jobless, likewise, would have to be far less choosy than now or face similar cuts: a job might offer up to 20% less than they used to earn, but they would have to accept it; young and single people would have to move anywhere within the country for work.

This could yet save Mr Schröder. He is determined not to become the federal republic's first chancellor to be denied a second term in office. With an upturn in support, he might do it. Even now, most polls suggest that the conservatives and their likely post-election allies, the Free Democrats, will not win an absolute majority of the vote. Everything would then depend on wheeling and dealing after the election. Even if the Social Democrats did not emerge as the biggest party, so long as they had done respectably they could still hope to form a minority government with the Greens, tolerated by the ex-communists; or a three-way coalition with the Greens and the Free Democrats; or even, conceivably, one, headed by Mr Schröder, with the Christian Democrats, though minus Mr Stoiber and his Bavarians of the Christian Social Union. The fact that such options, most formerly considered taboo by the Social Democrats, are

now being seriously considered indicates just how desperate Mr Schröder's party has become.

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Hungary's ex-spook politicians

You were another

Aug 15th 2002 | BUDAPEST
From The Economist print edition

Ministers left and right worked for "intelligence" in communist days

EPA

Medgyessy faces the committee

YOU won't usually find many Hungarian politicians in the capital in August. You will this year, thanks to two parliamentary investigations set afoot after it was revealed in June that Peter Medgyessy, prime minister in the Socialist-led government that won power in April's elections, was once a communist-era counterintelligence agent. The results are surprising.

One committee is looking at Mr Medgyessy's record; another at secret files that may reveal which other post-communist ministers had similar links. Unexpectedly, Mr Medgyessy and his team are emerging from the hearings pretty well. But for the centre-right opposition, notably Fidesz, the party of Viktor Orban, prime minister till April, they have been a body-blow.

Mr Medgyessy acted as an agent while working at the finance ministry in 1978-82. But he has stuck to his line that all he did was protect economic secrets and prevent the Soviet KGB from disrupting Hungary's application to join the IMF, which he was helping to prepare. Though some still doubt it, his story has not so far been seriously undermined. But this week Imre Mecs, the—pro-government—member of parliament leading the other investigation, said that, on the figures so far, fewer ministers in the two Socialist-led post-communist governments had past secret-service links (two and one, respectively, though it is unclear whether this includes Mr Medgyessy himself) than in the two conservative ones (five and four).

Conservative ministers may also have done nastier things than those held against Mr Medgyessy. Some—if leaks to the press are true—may have had links with the domestic intelligence agencies, snooping on neighbours and colleagues.

The probable explanation is that the left-leaning governments have included many former communist ministers or party officials—recipients, not writers, of the spooks' reports—plus a few ex-dissidents, likelier victims (by and large) than agents of the secret police. But among conservative ministers, a fair number in communist days were middle-ranking public servants; the sort of people whose help the spooks would hope to recruit.

The conservatives' response has not helped them. Their members on Mr Mecs's committee have walked out, talking of procedural irregularities. When the data-protection ombudsman ruled that no one should have data about him revealed without his consent, current ministers and those of the leftish government of 1994-98 rushed to give it. Ex-members of the conservative one of 1990-94 or Mr Orban's of 1998-2002 were slower.

Opinion polls suggest that Fidesz and the right have been hurt. Voters already knew that Mr Medgyessy was on the ruling party's central committee in communism's later days. But Mr Orban had portrayed his team as firmly anti-communist. To many, that now smells of hypocrisy.

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Terrorism in Spain

Shutters down on ETA's friends

Aug 15th 2002
From The Economist print edition

The government takes the first steps to a ban on the terrorists' political arm

Reuters

There was also a six-year-old in there

WHEN a bomb set off by your terrorist friends kills a child, it will not do just to talk of “tragic circumstances” and say that, while you “will not justify” the killing, you will graciously “analyse” why it happened. That is what Batasuna, the political arm of the Basque-separatist terror group, ETA, did last week after an explosion that killed a man and a six-year-old girl in a police barracks at a resort on the south-east coast. One week and another, mercifully victimless, resort explosion later, Batasuna learned the cost: the People's Party government, backed by the opposition Socialists and most public opinion, plans to recall parliament to start the process of getting Batasuna banned.

Under a new law passed for just this purpose, that means a parliamentary motion, which will then go to the Supreme Court for a ruling. With over 300 of the 350 seats, the two big parties face no problem getting the motion through. Even so, both are working to get wider support: from the far left, sundry regional “nationalists” and even the Basque Nationalist Party (PNV), which, though non-violent itself, is often accused of being the mild half of a soft-man, hard-man Basque-separatist duo.

The PNV-led government of the autonomous Basque region has long demanded that Madrid devolve to it the remaining functions—37 of them, it says—that it is entitled to but which are yet to be transferred. If not, and soon, it said earlier this year, it would take over these powers anyway. That was pure theatre. Now the centre says it will reopen talks about that—but expects PNV members in the central parliament to vote against Batasuna.

This too is political theatre, but it has a sharper edge. Batasuna has no reputation to lose, except among its own enthusiasts (though it managed to get 10,000 of them on to the streets of San Sebastian on Sunday, in protest against any ban). But the People's Party is eager to discredit the PNV as well. So ask its support for a ban, and its predictable refusal would have that effect. Which is, in fact, just what has happened.

It is less clear that banning Batasuna will help defeat ETA. Spain's prisons already hold some 500 proven or alleged ETA men (women, in fact, one in eight of them) or their active supporters. Regularly over the years some pro-ETA group or another gets jumped on. Yet, for all its murders, ETA still has supporters, and the threat of the San Sebastian demonstrators, “if you want war, you can have it”, is not to be taken lightly. A ban on their politics may push some into taking up guns instead. Even some firm supporters of a ban, like Spain's leading newspaper, *El Pais*, admit it could have unwelcome side-effects.

Few Spaniards have doubts, however. As huge protest marches have repeatedly shown, decent people are fed up to the back teeth with what *El Pais* rightly calls ETA's strategy of “blackmail and terror”.

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Terrorism in Greece

Better late...

Aug 15th 2002 | ATHENS
From The Economist print edition

Arrests of N17 members do not explain why it was immune for so long. Politics?

FEW Greeks feel the need for a thriller on the beach this summer. Pick up a newspaper or turn on the radio for the next instalment of real-time drama: the arrest—after 27 years when not one was caught—of members of November 17, a terrorist gang blamed for 23 murders and dozens of bomb and rocket attacks in that time.

Since the first arrest on June 29th, the police have pulled in 15 alleged N17 members, including French-educated Alexandros Yotopoulos, its suspected leader, nabbed at his villa on an Aegean island. Raids on hide-outs have turned up arms and explosives, and diskettes detailing N17 bank accounts and plans for future targets—among them NATO convoys to Kosovo from Salonika, and facilities being built in Athens for the 2004 Olympics.

Costas Simitis, the Socialist prime minister, is relieved: concern had mounted over security for the Olympics. He even had a pat on the back from George Bush, who called the arrests an “important contribution” to the war on terror. And Mr Simitis's Pasok party, lagging the centre-right New Democracy party as local elections approach, has seen its ratings rise.

Both parties are pushing the line that N17's members are more common criminals than terrorists. This ignores the nature of N17's victims (the first, in 1975, was the local CIA station chief), the long-winded ideological declarations it used to send to a leading newspaper after its attacks and the alleged role of Mr Yotopoulos. But with a general election expected late next year, the pretence suits both. Trials of N17 members are likely to start early next year and will last for months. Pasok, which used to have a Marxist charter, wants to distance itself from any reminder of its old beliefs; New Democracy wants no noisy left-right confrontation that might upset its chances of winning the election on the good old ideology of “throw the rascals out”.

Awkward questions remain. For the chattering classes, who rubbed shoulders with Mr Yotopoulos—under an alias—at fashionable cafés and gallery openings in Athens, the puzzle is how he avoided detection for over 20 years. Mere police incompetence, or high-placed political friends? N17's supposed head of operations, one Dimitris Koufodinas, is still at large. And the group has now promised fresh attacks. “Ridiculous,” declared Michalis Chrysohoidis, the public-order minister. Time will show.

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Charlemagne

The man Turks trust: Kemal Dervis

Aug 15th 2002
From The Economist print edition

Their economy needs a firm hand. His has been that. Will they be able to vote for it to be so again?

Get article background

“IT WAS very important to me to be top of the class, so that I would be chosen to carry the Turkish flag at the end of the week,” reminisces Turkey's freshly resigned former economy minister about his primary-school years on bucolic Buyukada island, in the sea of Marmara near Istanbul. Today, Kemal Dervis says his most cherished goal is to “establish a convergence of centre-left forces that would achieve the conditions under which Turkey can overcome its economic difficulties and pursue our road towards Europe and a modern and free society”.

Since announcing his departure from Bulent Ecevit's government last week, Turkey's most popular pro-secular public figure—he hates to be called a politician—has been seeking to do just that. Technocrat though he was and is, with no experience of down-to-earth electoral politics, he has been urging trade-union leaders and minor leftish politicians to forget their differences and unite (with him, though that is not how he puts it) against the likely victor of the general election on November 3rd: Recep Tayyip Erdogan, an ex-mayor of Istanbul, whose enemies call him, over his fierce denials, an Islamist.

It will be a surprise if Mr Dervis can unite the left. It is a shambles. Mr Ecevit supposedly is part of it. But when his ill-health sparked the collapse of his left-right coalition, and now an early election, the most prominent of eight ministers who quit, Ismail Cem, broke away from Mr Ecevit's Democratic Left to form his own New Turkey Party. Then there is the Republican People's Party, founded by Ataturk and now run by prickly Deniz Baykal. He sees only one fit leader for the left, himself.

Many modern-minded Turks would like to see Mr Dervis as prime minister. Certainly he is fit for that. He was recruited to the economy ministry from the World Bank in Washington 18 months ago to pull Turkey out of a financial abyss. He negotiated a gigantic bail-out package from the IMF and the World Bank, with a programme of fiscal and economic reform. For the first time, the central bank became truly independent. Money no longer grows by the trillion lira on printing presses. Politicians can no longer dip into state banks to fund their election campaigns. Much else has been begun, and all against tireless obstruction from some of Mr Ecevit's coalition partners. Deny it as he may, Mr Dervis is no infant in the art of political manoeuvre.

His real achievement, he says, was to sell the programme to the Turkish people. “By working closely with civil society, by making friends in the labour movement, we got people to see that it was in their interest.” The crisis was overcome—at a cost, he admits, that has hit the poor before the benefits turn up.

That is why the economy and Turkey's hoped-for membership of the European Union, not the supposed dangers posed by Islamic radicals and separatist Kurds, are set to be the main electoral issues. In the wrong hands, says Mr Dervis, meaning Mr Erdogan's, the economy could unravel again. It is also why some Turks and many foreign governments fancy him to lead Turkey.

But he has another quality. Scion though he is of a line of distinguished Ottoman pashas, he stands out among the politicians for being both modest and honest. And he insists that he has been a “social democrat all my life. I believe that humankind is one large family and while I'm fond of Turkey and patriotic, I've also always believed in the principles of the international social-democratic movement.”

Mr Dervis's free-market instincts may have come from his business tycoon father; but his progressive

ones he perhaps owes to his half-German, half-Dutch mother, who fled Hitler's Germany in disgust for a town in central Anatolia, where she taught English. And his skills in public finance? Well, one of his ancestors was instructed by the then Sultan Abdul Hamid I in the late 18th century to fix the already ailing Ottoman empire's finances. Like Mr Dervis, he did the job well. But the hapless pasha was decapitated, his severed head being duly placed in a gourd full of honey and exposed at the Topkapi palace in Istanbul, after he was implicated in a plot to overthrow the sultan.

Will he join the party?

Mr Dervis escaped that fate at the hands of Mr Ecevit. But he still avers that he is an economist, not a politician, and would rather be economy minister again in a government “where the centre-left has sufficient weight”. Which is very noble, but has not stopped him being courted by one political party after another. And for all his reputation, politically speaking he has to run for election. But with which party? Until he made up his mind this week, the best guess was Mr Cem's. But Mr Dervis dilly-dallied over any decision. Wimping out, his critics claimed. They were wrong: Mr Dervis feared that if he chose one party over others, rather than uniting the left he would split it even further, and in so doing assure Mr Erdogan of victory. This week, he had to admit temporary defeat: Mr Cem's party said it would fight the election on its own. Mr Dervis pledged to go on trying, but said he would not join Mr Cem, and in contrast praised Mr Baykal, who had promptly claimed to be ready for unity.

So now? If the left still will not pull itself together, Mr Dervis may yet, as he hinted earlier, retreat to academe. That would be a waste. He is popular enough, unlike Turkey's tired old cast of politicians, to launch a serious challenge to the charismatic Mr Erdogan. But, for Turkey, the real challenges will come after the election. “For all the economic problems, I believe the people will go where there is the greatest constructive realism and support those who have realistic long-term solutions,” says Mr Dervis. That belief may prove right or wrong, but they'd for sure be wise to. Turkey has lurched through fiscal chaos and wild inflation (1.64m liras, yes, that's millions, to the dollar) for far too long. It can become open and democratic—the current criteria—beyond the EU's insistence, nay its dreams, but is that the sort of economy you'd invite into a sober economic and monetary union?

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Insurance

Fire, flood and the equity markets

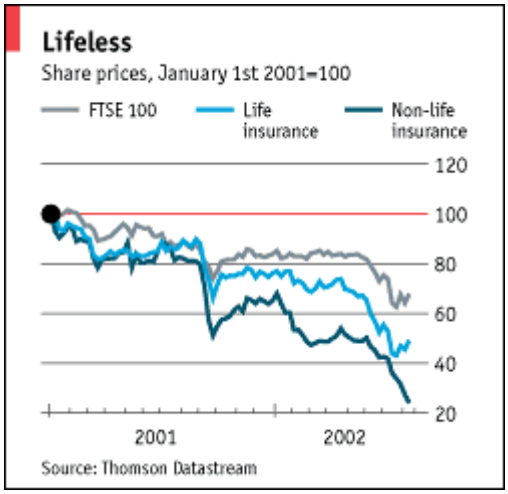
Aug 15th 2002
From The Economist print edition

Insurance companies are more important to Britain than they are to any other country's economy, which is why their troubles have such wide repercussions

IT IS unusual for the insurance industry to feel the hot glare of television cameras; but then these are unusual times in the insurance industry. On August 8th Royal & Sun Alliance (RSA), one of Britain's biggest insurers, was all over the news when it announced poor half-year profits, the closure of its life funds to new business and more than 1,000 job cuts; and on the same day Moody's, a rating agency, confirmed its “negative” outlook—the worst it ever gives—on British life insurers. And Ace, a Bermudan insurer and one of the most prominent underwriters at Lloyd's, the insurance market, announced plans to cut its business at Lloyd's by a third.

Shareholders and policy-holders are feeling the immediate consequences. Those who own shares in this reputedly “safe” sector have seen the value of their holdings fall by 54%, on average, since the beginning of the year. Non-life insurers have seen their average share price fall by almost two-thirds since January.

Rates for some property-and-casualty insurance are rocketing. Employers' liability insurance, for instance, which covers employers over claims for workplace injuries, has increased as much as six-fold for many businesses. Thousands of small companies are already trading illegally (employers' liability cover has been a statutory requirement since 1969) because they cannot afford or even find cover. On August 14th, the Federation of Small Businesses called on the government to set up a new insurer for employers' liabilities financed by taxes on insurance premiums.



Many of the life insurers' customers are unhappy, too. Equitable Life, one of the sickest of them, has recently slashed payouts again and increased penalties on those who attempt to cash in policies early. Trouble in the life insurance business matters a lot in Britain. Insurance is the nation's favourite savings vehicle:

Britain spends more on life insurance than any other West European country.

British insurers used to be the most successful in the world. Lloyd's was the pre-eminent insurance market, famed for its expertise, operating even in the remotest parts of the globe. Some of Europe's biggest insurers were based in London.

Things started to go wrong in the early 1990s when Lloyd's almost went bust thanks to huge pay-outs on claims ranging from pollution damage to natural disasters. It has survived, but in a different, smaller, form.

Still, by the end of the 1990s, British insurance was looking good, thanks to the bull market in equities. Some insurers had invested as much as four-fifths of their assets in equities, which at that time produced fantastic investment returns, so the insurers had more capital than they knew what to do with.

That was when the real trouble started. Over-confident, over-capitalised insurers took on too much risk at too low a price. Property-and-casualty insurers lowered rates to absurd levels, in particular in niche markets such as marine or aviation insurance. Their goal was to attract even more business with such ultra-cheap deals. Life insurers wrote more policies with guaranteed returns, which seemed a good idea to them at the time, but have now come back to haunt them.

Since the stockmarket started to slide, much of insurers' spare cash has gone. The spotlight is on life insurers, as some of them appear to be more fragile than the non-life firms. Ned Cazalet at Cazalet Consulting estimates that the life-insurance industry's excess capital shrank from £130 billion ($213 billion) in January 2000 to £30 billion at the beginning of the year, and to much less by now.

Life insurers' most immediate problem is a statutory solvency requirement. The Financial Services Authority (FSA) provided some breathing space on June 28th by relaxing the resilience test used to determine the capacity of life insurers' investment portfolios to absorb losses. Previously, an insurer had to be able to meet its financial obligations if the FTSE All Share Index dropped by 25% at any point in time. Now, insurers do not have to prove that they can withstand a sudden drop of 25%, but a 25% fall as compared with the FTSE's average over the past three months. Volatility, in other words, will not make them fail the test; only a sustained fall will.

Yet concerns over insurers' solvency have not disappeared. Insurers as a whole own about a quarter of the British equity market; the most vulnerable sector of the business, the life insurers, own 12%. Even if only weaker life insurers, such as RSA, Equitable Life and Abbey National, had to sell shares, the market would suffer. There have been rumours that the FSA is planning to relax the resilience test further. It has denied them.

Of course, British insurers are not the only ones in trouble. Concerns over German life insurers' health is such that the industry is currently discussing the creation of a pool that would provide funds to tie over insurers in dire straits. AXA, France's largest insurer, recently tried to talk up its plummeting share price by saying publicly that it had no plans to issue a profits warning, that it did not intend to sell equities and that its exposure to equity markets was anyway only 16%. American life insurers are big investors in corporate bonds, which is causing some worries. Moody's estimates that American life insurers lost $23 billion thanks to buying bonds of WorldCom, Enron, Tyco and the like. Mighty American Insurance Group (AIG) alone is estimated to have lost $1.8 billion thanks to bond defaults.

But British insurers are in deeper trouble than insurance companies anywhere else in the world, largely because, during the second half of the 1990s, they focused too much on winning business and too little on managing its risk. The industry is feeling the consequences. There has already been a wave of mergers—the biggest, in May 2000, created CGNU (now Aviva) out of Norwich Union and CGU. The industry will probably shrivel more. A report recently published by Swiss Re, a reinsurer, says that nearly half of the 86 syndicates, or businesses, that operate on the Lloyd's market, may close, and that several other London-based insurers are likely to shut down too. Their customers will not weep for them.

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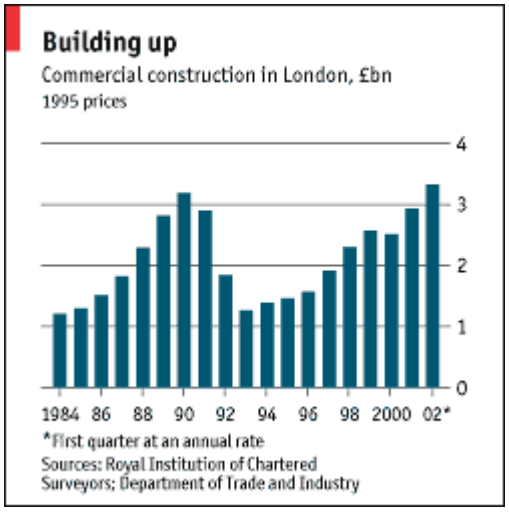
Commercial property

Cranes on the skyline, crashes on the horizon?

Aug 15th 2002
From The Economist print edition

As commercial property development booms, demand falters



CRANES interrupt London's skyline in every direction: even Sir Christopher Wren, architect of St Paul's Cathedral, must cede the view to Sir Robert McAlpine, the construction company, whose 12 cranes flank Wren's masterpiece. The Royal Institution of Chartered Surveyors estimates that commercial property construction reached £3.3 billion (at an annualised rate) in the second quarter of 2002, surpassing the peak of £3.2 billion which the business reached in 1990—after which very many developers went bust and bad loans to property companies sat heavily on the banks' balance-sheets.

Is the same likely to happen again? The parallels with the early 1990s are far from exact. Construction expenditures are higher than ever, but the volume of space being built is still well below the levels of 1989-90. Interest rates are unlikely to rise, and few expect Britain to go into outright recession. Much of the money being spent on construction now is for buildings that will not become available until mid-2003 or later, by which time economic conditions are forecast to improve.

Nonetheless, demand is faltering. A year ago, tenants would have to have paid £68.50 for a square foot of prime City office space. Today they pay £63 ($96). Jones Lang LaSalle, a property agency, calculates that the demand for commercial space in Central London is about 30% below its average for the past five years.

There are plenty of concrete examples—as well as many in steel and glass—to confirm the story the statistics tell. Investment banks, in particular, are in full “disposal mode”, victims of a stockmarket bubble turned to bust. In early 2001, Lehman Brothers signed up for 1m square feet in Canary Wharf, but is now looking to sub-let some of its existing square footage in Broadgate. Citigroup in Canary Wharf has put 300,000 square feet on the market, but would probably accept offers for up to 600,000 square feet. Analysts fear that Docklands' vacancy rates could reach as high as 20%. Large chunks of space are also available from banks in the City.

Amid the gloom, there is some cheer for developers. Although the FTSE's travails have clipped the wings of some large occupiers, they have made real estate a more attractive asset for investors. And while London may be overbuilt, demand for property, especially retail space, is stable, and even strong, elsewhere in the country. Perhaps it is time the cranes migrated northwards.

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Woodland burial

Going wild

Aug 15th 2002
From The Economist print edition

An ecologically friendly solution to overcrowded cemeteries

MENTION digging up graves and most people start to get a bit twitchy. But exhuming human remains from old, untended graves whose lease has expired is exactly what many cemeteries across Britain are going to have to start doing if they want to stay open. At present, that is illegal, but Ian Hussein, director of the City of London Cemetery in Manor Park, believes that, unless the law is changed and cemeteries are allowed to re-use graves, within a decade or so burial will be unaffordable for most Britons. The average price of a burial has already risen from £893 in 1991 to £2,048 ($3,105) in 2000.

The Church of England has been digging people up for centuries: churches run their cemeteries under their own rules. Municipal cemeteries, however, answer to the Home Office. Some of them are already quietly exhuming bodies by the acre in order to sell off the land for other uses. Weirdly, that is perfectly legal, while, under current legislation, turning old graves into new ones is not. A Home Office consultation document has been promised.

In the meantime, another development is helping to relieve some of the pressure on Britain's overcrowded cemeteries. Woodland burial—usually with a coffin made from a biodegradable material such as willow or cardboard—is an increasingly popular alternative to the traditional western-style funeral involving a brisk cremation or a short lease in a municipal cemetery. Instead of a headstone, a typical woodland grave is marked only by a tree.

The first woodland burial site in Britain opened in 1993. According to Stephanie Wienrich of the Natural Death Centre, a London-based charity, there are now more than 160 woodland and nature-reserve burial grounds open or currently in development across Britain. Most are run by local authorities or as businesses by farmers or private land owners. Two are run by the Church of England. The largest woodland burial site in Britain, in Turriff, Aberdeenshire, which has room for 12,000 souls, opened last week.

“The popularity of the woodland-burial concept,” says Ms Wienrich, “reflects a growing preference for personalised, non-religious funerals, and the idea of being returned to nature when you die.” The baby-boomers and 1960s flower children are getting to a certain age now, and many are looking for “alternatives” in death just as they may have done in life. A woodland funeral can be as idiosyncratic (or, for that matter, as conventional) as you like.

Farmers, too, welcome the growing interest in woodland burial as a means of diversification in these hard times. They own the land already; the administration and nitty-gritty of grave-digging and funeral services can be outsourced; and the maintenance costs are practically nil. Turning an unused field over to woodland burial is money for old bones.

The City of London Cemetery created a small woodland site in 1994. Though very much in favour of woodland burial, Mr Hussein insists that it must not be seen as an easy solution to the problems currently facing Britain's overcrowded cemeteries. The demand for traditional burial—complete with fancy coffin, stone monument, space for floral tributes and so forth—is still very strong. It will, he says, take many years for that culture to change, and for the woodland approach to take off. But there's no reason why it shouldn't. The grandeur of an arboreal memorial is pretty hard to beat. Why settle for pushing up daisies when you can push up a mighty oak?

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Public toilets

Bog standards

Aug 15th 2002
From The Economist print edition

The long drop in public-toilet provision

A FORMER toilet in south London is to be turned into a luxury flat, it emerged this week. The agent, Tony Wood, says the Edwardian property has many original features, including a sign saying “Lavatories” carved on the wall. With its central location (between a main road and a train station), Mr Wood thinks it will be a snip at £125,000 ($193,000). He speaks from experience: down the road in Brockley, his firm has set up office in another disused loo.

Many public loos occupy prime sites; thanks to the property boom, local councils have found themselves sitting on a valuable asset. In the past eight years, 47% of public conveniences in Britain's cities have closed: that leaves one for every 20,000 residents. “We are becoming a third-world country in toileting,” laments Richard Chisnell, director of the British Toilet Association. One consequence, he maintains, is that street fouling has reached “medieval proportions”.

Mr Chisnell is well placed to judge. The BTA is a founding member of the World Toilet Organisation; last year, he attended the first World Toilet Summit in Singapore. “Good toileting,” he says, “is a global issue.” Disturbingly, while some countries take this issue seriously—Delhi even has a toilet museum, whose magazine is aptly titled *Sanitation Digest*—bursting Britons may soon be in for an even tougher time. By October 2004, local authorities will be required to make all their loos accessible to disabled users. But they have no obligation to provide any at all, and Mr Chisnell expects many will be closed rather than converted.

A few councils still lavish attention on their lavatories. On the Isle of Bute, one toilet boasts attendants dressed in Victorian costume. East Lothian's splendid loos attract business from miles around, and they have the visitors' books to prove it. Most councils, though, are delighted to dispose of Victorian toilets; they prefer Automatic Public Conveniences, which charge admission and are cheap to maintain. In central London, a Dutch contraption called the Urilift—a remote-controlled urinal which pops up at night and disappears at dawn—is making its debut next month.

The BTA wants to see national standards and statutory requirements put in place. It plans to establish a toilet academy, in an old sewage works in Winchester, to promote best practice. It already runs the prestigious Loo of the Year award: the current holder is a pub in London's Docklands. Mr Chisnell says winners see their turnover shoot up, which just goes to show the pulling power of a decent loo.

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Scottish population

Bairns needed

Aug 15th 2002 | EDINBURGH
From The Economist print edition

Scotland's shrinking population has political ramifications

WHILE the south-east of England agonises about congestion, Scotland's wide open spaces look like getting emptier still. The results of the 2001 census, due out next month, are expected to confirm a long, slow decline.

According to the Office for National Statistics (ONS), Britain's population, 59.8m in 2001, is expected to grow to 64m by 2021. But Scotland's population, now about 5.1m, is forecast to shrink gradually, falling below 5m in about 2018.

Recent economic news seems bound to worsen this trend. According to the Scottish Executive, the devolved government, Scotland's economy shrank by 1% last winter and this spring, which means a recession. These figures fit a gloomy pattern: Scotland's growth rate over the past decade averaged 1.9% a year, while Britain's averaged 2.3%.

A shrinking population is both cause and effect of low economic growth: people move away from slow-growing areas, thus further slowing the growth. That's one of the reasons why Scotland's population has been stagnant over the past half-century, while Britain's as a whole has grown. But emigration is not necessarily the main problem looking ahead. The ONS forecasts assume there will be no net emigration in the future. The big problem now is that Scottish women are producing fewer babies than they used to, and fewer children than other British women.

A country's fertility rate (the number of children produced by the average woman) needs to be 2.1 for the total population to remain constant. Britain's fertility rate is currently about 1.64, way down on the 1960s fertility rate of more than 2.5 thanks to modern contraceptives. An expected influx of 135,000 people a year more than makes up for Britain's low birth rate, so the population will go on growing.

Scotland's fertility rate, at 1.48, is well below the British average. Nobody knows quite why Scottish women seem reluctant to reproduce. Paul Boyle, a professor of population geography at St Andrews university, says that Asian immigrants (who tend to have large families) are a smaller percentage of the Scottish than the English population, but that is not enough to account for the difference. Some suggest that Scottish emigrants are young and fertile, whereas immigrants tend to be past child-bearing age. But that ought to be counter-balanced by the fact that more Scots are working class, and they tend to have more children than the middle classes.

Scotland's low birth-rate may have political consequences. The problems of an ageing population, common to all European countries, will be that much sharper north of the border. Demand for health services and residential care services for the elderly, for example, will rise faster.

Since the Scottish Executive decided that it would pay old people's personal care costs (unlike Tony Blair's government, which is not paying these bills south of the border), Scotland's welfare bill is likely to rise. At the same time, there will be fewer working-age people. Moreover, argues Robert Wright, an economics professor at Stirling University, Scottish employers will find it harder to recruit young workers, pushing down productivity.

All this implies that, relative to the rest of Britain, the Scots will pay fewer taxes into the British treasury and make more demands on it. That will further strain relations between Scotland and England, whose politicians, especially in the north, increasingly resent Scotland's disproportionately large share of public spending. More bairns, please.

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Low-cost airlines

Fly me, I'm cheap

Aug 15th 2002
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The price of flying on a low-cost airline

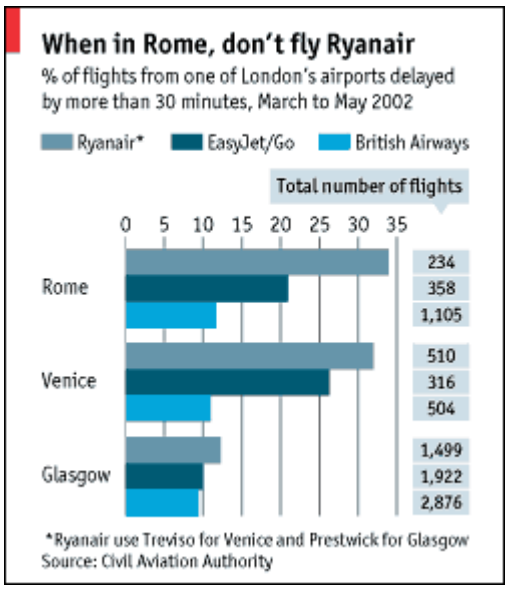
Get article background

PHIL KENNY, one of *The Economist*'s graphic designers, booked this month to fly with nine friends from Stansted to Nimes. Their Ryanair flight was delayed an hour because of a broken baggage conveyor belt. The truck carrying their baggage then crashed into the plane, ripping a small hole in the fuselage. A replacement had to be flown in from Dublin. When the plane finally arrived at Nimes five hours late, some of the group's bags were missing. “It was a joke from start to finish,” says Mr Kenny, with unwarranted good humour.

Nobody in their right mind would fly on one of Britain's low-cost airlines and expect to be cosseted. No free food or drink, no assigned seats, no transfers and no compensation for delays or lost baggage. Ryanair, which carries more than a million passengers a month, has so little faith in its timetable that it advises customers not to book connecting flights.

Cheap they certainly are. Ryanair's average fare per 600 kms, say industry analysts, is £34, compared with easyJet's £45, Go's £55 and British Airways' £108.

Cheerful they aren't, if you listen to this summer's crop of horror-stories. The problems are largely the result of success. With passenger numbers expanding at a break-neck 60% a year, staff and equipment shortages have led to a growing number of delays and cancellations. The punctuality record is mixed. On some routes, the low-cost airlines are as good as the full-fare scheduled carriers. On others, such as Rome and Venice, they are significantly worse (see chart).



The low-cost carriers are able to offer low fares only by sweating their assets. EasyJet and Ryanair fly their Boeing 737s for 11 hours a day, four hours longer than BA. Their pilots fly 900 hours a year, 50% more than BA's pilots. The budget airlines allow only 25 minutes between flights to offload one set of passengers and load another, less than half the time of its scheduled full-fare rivals. EasyJet cheerfully admits to having about “one and half planes' worth” of spare capacity compared with the dozen planes BA has on stand-by at Gatwick and Heathrow in case of problems. Ryanair's ground handling charges of £12 per passenger are roughly a quarter of those of BA.

Expanding at such a pace in such a fiercely competitive business leads to problems. EasyJet, challenging Ryanair for the leadership of the pack after its acquisition of Go, admitted this month that it was having to scrap a new flight-crew roster because it was “rubbish.” The group's operations director, Vilhelm Hahn-Petersen, has written to the company's pilots acknowledging that they were being overworked and that the airline would have to scale back its ambitions in the short term.

Claims by the British Airline Pilots Association that safety is being compromised are, however, fiercely denied. Earlier this summer an anonymous air-traffic controller filing a report to Chirp, the industry's confidential whistle-blowing agency, claimed that pilots of low-cost airlines were cutting corners to achieve flight timetables. The founder of easyJet, Stelios Haji-Ioannou, further fuelled the safety debate

by expressing doubts about Ryanair's use of 20-year-old aircraft on some of its routes, pointing out that though they flattered profits in the short term, they put the future of the airline at risk in the event of an accident. These remarks set off a furious row with Michael O'Leary, the boss of Ryanair, telling his rival to stop whingeing. “Those of us who sell the lowest air fares just get on with it,” he said.

Ryanair, which is phasing out its older Boeing 737s over the next three years, has had an unblemished safety record in its 18 years of operations. But it, like every other low-cost operator, is only too aware of the fate that befell an American airline, ValuJet, which went out of business after one of its planes crashed in a Florida swamp in May 1996 killing all 110 people on board. The low-cost airline business is not for the faint-hearted. As Mr O'Leary notes: “There's a challenge every day in this business not to do something stupid.”

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Environment

Meacher's moment

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The green who came in from the cold

NOT since the glory days of the early 1980s when Labour's cultural revolution was in full swing and he was running for the party's deputy leadership as “Tony Benn's vicar on earth” has Michael Meacher been the centre of quite so much attention. Mr Meacher, who has been minister for the environment since 1997, was mysteriously omitted from the 70-strong British delegation to the Earth Summit in Johannesburg later this month, allegedly on the orders of the government's media supremo, Alastair Campbell.

Given that Mr Meacher these days only rarely breaks cover, the outcry that greeted this revelation was as strident as it was unexpected. If just one person should go to Johannesburg, protested Britain's green lobby, it should be Mr Meacher, the only man in government who really understands the issues. Friends of the Earth, no less, was prepared to pay the minister's air fare. It didn't take long for Downing Street to change its mind, speedily sending Mr Meacher an invitation, insisting that the list excluding Mr Meacher had not been the “final” one.

The really surprising thing is not so much that Mr Meacher should have been the intended victim of this crude snub, but that, despite some obvious handicaps, he has established himself as one of the government's great survivors. Unlike some others with a hard-left past, Mr Meacher has neither recanted his socialism nor felt it necessary to clasp New Labour to his bosom. Although a minister in the 1974-79 Labour government and a senior member of the shadow cabinet throughout the long years in opposition, Mr Meacher, who will be 63 this year, expected little in the way of preferment from Tony Blair, on grounds of both age and ideological dodginess (he has the distinction of apparently being the only Labour minister on whom the CIA keeps a file). But although Mr Meacher shakes his head in puzzlement when asked about the “Third Way”, he has a sort of apple-cheeked, bespectacled innocence that seems to disarm even the most praetorian Blairite.

It is also perhaps an indication of the government's lack of green credentials that it has been happy to appoint and then keep someone so far from its centre of gravity in what has become an important post. However, with few friends at court, Mr Meacher has ploughed his lonely (non-genetically-modified) furrow with skill and diligence. His mastery of his brief, his patent sincerity and his willingness to stand a little aside from the government's lust to pave over the south-east has won him the respect of greens. He has even dared to set tighter conditions for GM crop pilots, which are due to be evaluated next year, than the “pro-science” Mr Blair would have liked.

But while Mr Meacher is more than happy to spout about pollution-apocalypse, he saves his real passion for things that are both more prosaic and immediate. He is, for example, campaigning vigorously for a tax on the horrid plastic bags doled out in their millions by supermarkets. He would also love to see councils across the country employing “environmental wardens”—uniformed officials who would have the power to apprehend and fine graffiti sprayers, litter louts and the careless owners of incontinent dogs. The prime minister is apparently all in favour of the idea and has agreed that the fines could be used to pay the wardens' salaries. At the Home Office, David Blunkett is said to be impressed with the authoritarian potential of Mr Meacher's plans.

With the sudden media interest in him last week, and with Mr Campbell on holiday, Mr Meacher took his opportunity to be ever so sweetly disloyal, regretting the government's failure to tackle environmental issues with greater vigour and describing himself at one point as “a lone voice in the wilderness”. It will be interesting to see if Mr Meacher has now acquired the same sort of licence to speak his mind as Clare Short, the feisty overseas development minister. If so, it will be a paradoxical achievement for whoever decided that the forthcoming jaunt to Johannesburg should be Meacherless.

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Reforming corporate governance

In search of honesty

Aug 15th 2002 | LONDON AND NEW YORK
From The Economist print edition

Will the new fashion for swearing oaths make company bosses tell the truth?

THE certification of company accounts by senior executives should be a non-event. After all, financial statements were always supposed to be true and complete, and lying has long been deemed fraudulent. But in the wake of Enron, WorldCom and a slew of other scandals, America no longer trusts its corporate leaders to tell the truth without being warned by the sound of prison doors slamming. Thus, new rules requiring chief executives and chief financial officers to sign off on their accounts have become the stuff of headlines.

All the headlines this week concerned August 14th, the SEC's deadline for the bosses of 695 listed American companies with annual revenue of more than $1.2 billion to swear by their financial statements or admit to problems. They are not the only ones under the microscope. Another 250 or so firms (those that do not have a calendar year-end) are expected to vouch for their numbers later in the year. And under America's new Sarbanes-Oxley act, the senior executives of all 14,000 firms listed in the United States, including those based overseas, will have to certify their accounts from August 29th.

As people logged on in their thousands to the SEC's website to check which companies had made the cut—and as the treasury secretary, Paul O' Neill, called business honesty “the new patriotism”—it became clear that several firms would unpatriotically miss the deadline. Not surprisingly, the battered energy and telecoms sectors produced the most laggards (including CMS, Dynegy and Qwest). A big trucking group, Consolidated Freightways, also asked for more time. The penalties these companies face are still not clear.

Numerous companies filed but added caveats. Among these was AOL Time Warner, which noted possible revenue overstatements at AOL. And several firms filed restated earnings, including Interpublic and Household International. Because so many companies filed at the last minute, bad news buried deep inside may take weeks to emerge.

Those who certify dodgy accounts are not necessarily doomed to years in prison. Terms in the oaths such as “wilfully” and “knowingly” appear in enough places that clever executives—or those with clever lawyers—should have little problem escaping punishment by playing dumb. Just to make sure, in recent weeks wily bosses have been forcing their middle managers to sign documents saying that the information they have sent up to the CEO's office is accurate. If a company blows up, this will allow the

boss to blame the small fry. The positive aspect of this is that, by signing off on their accounts, the underlings are being given a strong reason to resist pressure from above to cook the books, says Robert Pozen, a professor at Harvard Law School.

The oaths are only the first wave in a flood of new regulations enveloping companies in America. The New York Stock Exchange (NYSE) and the Nasdaq have brought in new listing standards, and Congress has passed the 130-page Sarbanes bill. Putting it into practice will require thousands more pages of legislation. Companies may have to change the composition of their boards radically, as well as their relationship with their accountants.

The new rules are aimed at restoring the quality of disclosure by preventing the harmful conflicts that were evident in the most spectacular recent bankruptcies. For this approach to succeed, management has to take its responsibilities as a fiduciary seriously; accountants and bankers need to ensure the disclosure is accurate; and investors must actively monitor their interests, says Peter Clapman of TIAA-CREF, a large fund manager for teachers. In recent years, managers simply stopped acting in the interest of shareholders, and accountants and bankers stopped requiring accurate reports. “The disclosure became worthless,” says Mr Clapman.

The new listing requirements of the NYSE and the Nasdaq require firms to get shareholder approval for all stock-option plans. They must also have a majority of independent directors on their boards, and only independent directors on the audit committee and the committees that select chief executives and determine pay.

For its part, the Sarbanes act prohibits companies from providing subsidised loans to executives, and requires bosses to reimburse incentive-based compensation if profits are found to have been mis-stated. Executives will also have to report sales of shares more quickly. Furthermore, the bill states that company lawyers serve the company itself, not the managers, and thus have a duty to report transgressions to the board (which should, remarkably enough, have at least one person who understands accounting). Accounting firms will have to rotate the partners supervising audits, and accounting partners will no longer be able to jump directly into upper management at client companies.

Yet there is suspicion that the changes will be less effective than they appear. Enron's audit committee, after all, was chaired by a distinguished accounting professor. Lawyers, bankers, accountants and board members have always, in theory, worked for shareholders, not management. Moreover, the new rules fall short in a number of areas: for instance, a mandatory rotation of auditors would have guaranteed a change in oversight.

Stricter enforcement may compensate for such shortcomings. The Sarbanes act in effect replaces the self-regulation of accountants with a new public accounting oversight board, a majority of whose five board members will be from outside the industry. Congress, meanwhile, has suddenly decided that there is more political mileage in funding the SEC than starving it. The commission's budget is likely to grow from $438m this year towards $600m. The SEC's lawyers are among the worst paid in Washington, DC. “These guys have been overwhelmed for years,” says Joseph Grundfest, a former SEC commissioner.

They sinned, we get punished

While all this has been accepted in America as necessary medicine for the country's corporate ills, it has caused anger and dismay abroad. That is because the Sarbanes act turns out to apply in full to all companies with a stockmarket listing in America, regardless of where they are incorporated, and regardless of how exemplary that country believes its rules on corporate governance and auditing to be. Senior executives of some of the largest non-American companies will have to certify their accounts. Like their American peers, they will have to pay back their bonuses if the company restates its numbers as a result of misconduct, and they will be banned from borrowing from their employer.

Foreign auditors are also fingered by the act. Those that give an opinion on the financial statements of a company with an American listing must register with and obey the new accounting oversight board. Most controversially, foreign auditors will have to send audit working papers on their clients to the board if ordered to.

“We are not some sort of corporate backwater,” says Dame Judith Mayhew, chairman of the Corporation of London's policy and resources committee, who complains that the SEC is trying to set itself up as a global regulator. The European Commission has objected forcefully to the extra-territorial impact of the

act.

For all the huffing from national regulators, however, international companies are likely to accept the new rules with good grace. It is, after all, their own choice to raise money in American capital markets. “We will express our concerns privately,” says Geoffrey Mitchell, chief accountant of Barclays, a British bank, “but it would not give the right message to investors for us to accept only grudgingly.” It can be argued that the lack of any system for enforcing accounting standards in some European countries, such as Germany, invites interference from overseas.

Most galling for countries outside America are the parts of the act that conflict with domestic law. In Germany, for instance, employees must have a place on the audit committee of a company, a presence that would flout the act's independence rule. At the moment, says Alex Cohen of Latham & Watkins, a London law firm, it is unclear to what extent legislators intended to push American jurisdiction so deeply into other countries. Much still rests on the various exemptions and interpretations that the SEC will make in coming months. It could, for instance, exempt foreign accounting firms from the obligation to register with the new oversight board, though since it can only do so “in the public interest” or “for the protection of investors”, accounting firms worry that it is unlikely to.

One part of the act, in fact, makes a remarkable concession to other countries' ways of doing things. Its requirement that finance chiefs certify that the periodic report “fairly presents” the company's financial condition makes no mention of American generally accepted accounting principles (GAAP). From now on, executives will no longer be able to avoid legal action simply by following the letter of America's accounting rules. Instead, they must also consider overall fairness, an accounting principle that holds sway in Britain. In this crucial respect, American financial reporting is catching up with Europe, rather than colonising it.

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News Corporation

Rupert the invisible

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From The Economist print edition

Looking healthy, relatively speaking

IF DISCRETION is the new currency for media moguls, then perhaps Rupert Murdoch's silence these days should be no surprise. At a time when media bosses not much more than half his age are being evicted, the famous mischief-maker is an unlikely model of reliability and stability in troubled times. Mr Murdoch has something to feel smug about, and not only because he is secure at the helm of News Corporation, the company his family controls. This week's annual results revealed a relatively robust media company, confirming News Corp's position, along with Viacom, as one of the hardier survivors of the media downturn.

At first glance, the company's pre-tax loss of $5.7 billion for the year to June 2002 scarcely looks reassuring. Yet this was chiefly to do with big write-downs, including of sports contracts in America; its stake in KirchMedia, a bust German group; and its investment in Gemstar-TV Guide, a provider of television guides. Compared with the *euro*11 billion ($10 billion) write-down and *euro*12.3 billion loss for the first half alone announced this week by Vivendi Universal, a media rival, News Corp's loss is almost modest. Vivendi's shares fell 25% on the news.

Moreover, News Corp's underlying performance is healthy. Year-on-year revenues grew 10% to $15.2 billion, and net profit before write-downs was $636m, down just 8%. While the company has traditionally traded at a discount thanks to its complicated structure, News Corp's shares have held up better than those of its more troubled rivals (see chart 1).

What has News Corp done right? Its first achievement was to fail to “get” the Internet. At the height of the dotcom frenzy, News Corp was pummelled for being slow to invest in online media. The few punts it did make, such as on e-partners, its $300m new-media investment business, were ill judged—but at least relatively small. By jumping in late, the company saved itself from far worse damage.

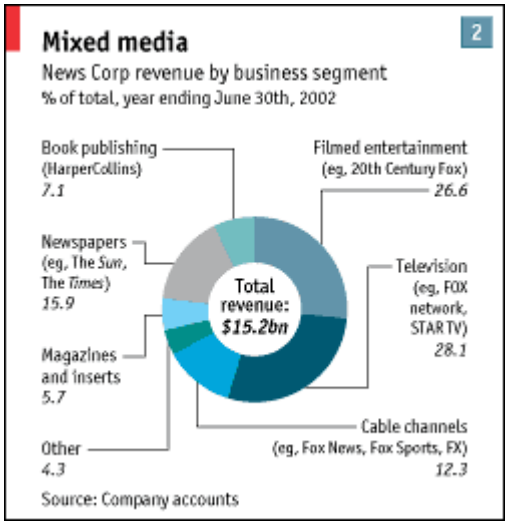
Its second feat was to have made some of its dull old media assets sparkle. Under Peter Chernin, Mr Murdoch's right-hand man, the star performers have been such businesses as television stations, film, publishing and syndicated television shows, all of which were being written off not so long ago as no-growth businesses.

Films, for instance, are enjoying a boom (see article), and 20th Century Fox, News Corp's studio, has released some strong movies recently, including “Star Wars: Episode II” and “Ice Age”. Fox has also been milking the surge in DVD sales, using current releases, its film library and even archived television series, such as “The X-files” and “The Simpsons”. Overall operating profit at the group's film division shot up by 78% to $473m.

The group's branded cable-TV channels—such as Fox News and Fox Sports—are also defying the gloom, with operating profit up 88% to $199m. In the first quarter of this year alone, according to Morgan Stanley, profit margins at this division rose from 7% to 16%. Fox News now routinely gets better ratings than CNN, and has been increasing its ad rates accordingly.

A third reason for News Corp's resilience is its diversity (see chart

2). Though heavily exposed to the advertising cycle, its mixed bag of assets has helped to cushion the blow. The collapse in revenue at the FOX television network, for instance, has been partially offset by increasing profitability elsewhere. Though News Corp does not consolidate BSkyB, of which it owns 36%, the British pay-TV operator has just turned to profit. And a weaker performance by the group's newspapers, which include Britain's *Times* and *Sun*, was offset by strong growth at HarperCollins, its book publisher.



Added to all this, News Corp's finances are now in reasonable shape. During the downturn of the early 1990s, the company teetered on the edge of bankruptcy. Stung by that experience, Mr Murdoch has become a more cautious gambler. News Corp has restructured its balance sheet so that it carries only long-term debt. Furthermore, over the year to June, the company cut its debt by 8% to $8.7 billion, while boosting its cash by 26% to $3.6 billion.

News Corp still has plenty of headaches. Stream, its Italian pay-TV operation, is still bleeding money—it lost News Corp $35m in the year to June—and Mr Murdoch is stuck in a stalled negotiation with Vivendi over his agreement to buy the French group's Italian pay-TV company, Telepiu. News Corp has also had to abandon—for now—its global satellite-TV strategy after failing to buy DirecTV, the largest American satellite-TV operator, last year.

All the same, insiders describe the mood at News Corp as one of “quiet satisfaction”. Smugness, they insist, is going too far. “We've all made mistakes,” said an unusually reticent Mr Murdoch this week. Even media moguls can be sensitive to charges of corporate hubris.

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Cinema

If you film it, they will come

Aug 15th 2002
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A rare bit of good news for media firms: box-office receipts are roaring ahead

AMID the melancholy in the media industry these days, one piece of cheering news stands out: cinema box-office receipts are booming. So far this year, according to Exhibitor Relations, a research group, the box-office take in America is up 15% on the same period in 2001—a year which itself broke records, with receipts up by nearly 10%, to $8.4 billion. This is not just because of higher ticket prices: admissions are up by 11% so far this year, and by around 30% in the past decade.

As good as it gets
Top ten US opening weekends
box-office receipts

	Film	$ million	Release date
1	Spider-Man	114.8	2002
2	Harry Potter and the Sorcerer's Stone	90.3	2001
3	The Lost World: Jurassic Park	90.2*	1997
4	Star Wars: Episode II	80.0	2002
5	Pearl Harbor	75.2*	2001
6	Austin Powers in Goldmember	73.1	2002
7	Mission: Impossible 2	70.8	2000
8	Planet of the Apes	68.5	2001
9	The Mummy Returns	68.1	2001
10	Rush Hour 2	67.4	2001

Source: *Variety* *Holiday weekend

Why are people flocking to the big screen? Certainly, 2002 has brought blockbuster films, such as “Spider-Man” and “Star Wars: Episode II”. And the autumn will bring still more, including a follow-up to both “Harry Potter” and “Lord of the Rings”. Such mega-hits can skew the numbers. Of the 450-odd Hollywood films released in any year, the top ten bag about 30% of all box-office takings, according to David Hancock of Screen Digest, a research group.

Indeed, part of the reason for the box-office boom is that the big studios now pump up a handful of “event” movies each year with vast marketing budgets, designed to create a buzz worldwide. The average marketing cost for a Hollywood film has nearly tripled over the past decade. Sony, for instance, spent some $50m promoting “Spider-Man”, and a similar sum on “XXX”, its latest heavily hyped action flick.

The idea is to hit hard, early. And it seems to be working. Eight of the ten films with the highest-ever opening weekend box-office receipts were released either this year or last (see table). In 1998, the average film made 34% of its total revenue in the first week of its release; now, the opening week accounts for nearly half a film's overall take, according to Dade Hayes of *Variety*, a Hollywood trade paper. The jackpot, when hit, is huge. “Spider-Man” has already brought in $773m at the box office worldwide, having cost about $130m to make. This figure will be dwarfed by the income it makes from video, DVD, television rights, video games and so on.

There are other explanations for cinema's renewed popularity, including comfier seats and a quest for escapism, or for communal entertainment, in troubled times. It could also be that the Hollywood hype machine is creating a sense of scarcity. By saturating screens, each movie is given less and less time to prove itself. By the time many people hear about a sub-blockbuster film, the local cinema is probably showing something else. As Hollywood's obsession with the opening weekend filters into the general consciousness, cinema-goers may be rushing to the big screen for fear of missing the new release altogether.

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Airlines in America

Landing with a bump

Aug 15th 2002
From The Economist print edition

US Airways will not be the last airline to slide into bankruptcy

Get article background

CRIPPLED by the terrorist attacks on September 11th and hampered by high costs, US Airways finally adopted one of the American airline industry's most popular and controversial ploys on August 11th, filing for Chapter 11 bankruptcy. The airline admitted that it needed more than just time to put its house in order. As the dominant carrier on America's east coast, it was hit hard by the aftermath of September 11th. The decision by the federal authorities to shut down Ronald Reagan Washington National Airport for three weeks after the attack threw its business into a spin.

US Airways made a loss of $2 billion in 2001 and has struggled ever since. Most of its staff realised that drastic action was needed when the company recently announced a loss of $248m for the second quarter, its eighth quarterly loss in a row. That was one reason why, even before filing for Chapter 11, the company had managed to do deals with unions representing the pilots and flight attendants to reduce costs. A third union, representing 12,000 mechanics and service workers, will vote on further concessions on pay and conditions by the end of the month.

If that deal goes his way, David Siegel, US Airways' chief executive, will get the room for manoeuvre that he needs to repair the airline's finances. Also helping will be a federal loan guarantee of $900m from the Air Transportation Stabilisation Board (ATSB), formed after September 11th to help keep America's airlines aloft.

US Airways' tribulations have cast light on another airline in a similar plight: United Airlines. Like US Airways, United is trying to secure a federal loan guarantee, but so far without success. Since the ATSB has so far awarded little of the $10 billion or so in aid at its disposal, United is unlikely to go away empty-handed. But it may have to wring more concessions from its employees and creditors. This week, United's parent, UAL, said it may be forced to follow US Airways into bankruptcy if it cannot drastically cut costs.

American Airlines, the world's largest carrier, is not immune to the troubles either. Like others, it is redoubling its efforts to cut costs. On August 13th, the airline said it would shed 7,000 jobs by March 2003 and retire 74 aircraft. These and other steps should save the airline more than $1 billion a year. One consolation is that, for now, American has a stronger balance sheet than many of its competitors. In July, the airline raised $500m by issuing new bonds to investors.

American, United and other mainstream airlines continue to feel the pressure from low-cost carriers, led by Southwest. Some think the budget airlines' rise will spell doom for traditional carriers. But Hubert Horan, author of a recent study published in *Aviation Strategy*, an industry newsletter, is more sanguine. He sees the low-cost carriers weakening, rather than destroying, the big airlines. For one thing, hub-and-spoke arrangements, dominated by the big airlines, are still the most economical way to offer frequent air service in most markets. Even though some low-cost carriers are now flying between big hubs (as opposed to more scattered “point-to-point” locations), Mr Horan doubts they will ever conquer that market.

The real problem building up in recent years, he argues, was not low-cost competition, but the reckless expansion of the big carriers between 1996 and 2001, when they added 3% more capacity each year in a mostly mature market. Excess capacity led to price-cutting for leisure travellers to bring in marginal revenue. Attempts to compensate for this by raising business fares met with strong resistance.

Mr Horan concludes that there was around 15% over-capacity in the American sky before September 11th. The terrorist attacks merely made an awful situation worse. Their main impact was probably to speed up what was coming anyway.

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Monsanto

Genetically modified company

Aug 15th 2002
From The Economist print edition

Has Monsanto learned its lesson since causing a stir in the late 1990s?

“AS A man sows, so shall he reap,” is a biblical lesson that really means something in the agricultural chemical and seed business, where profits critically depend on timely plantings and rich harvests. One firm, however, knows far better than most what it is to reap the whirlwind: Monsanto, a leading purveyor of genetically modified (GM) crops.

Two years ago, Monsanto was arguably the world's most controversial company, praised by those who see a future of environmentally friendly farming and healthier diets in high-tech crops, and damned by others who consider them promoters of ecological destruction and corporate control of the global food supply. Under siege from anti-GM protestors and heavily indebted after a $5.3 billion acquisition spree, Monsanto found temporary shelter under the roof of Pharmacia, an American drug company that bought the embattled firm for its successful pharmaceutical division, Searle.

In 2000, Pharmacia floated 15% of Monsanto on the stockmarket and announced plans to spin off the rest by the end of this year. Last month, Pharmacia itself was snapped up by Pfizer, an American rival, and the Monsanto sale was pushed forward. This week, Pharmacia handed its remaining stake to its shareholders, to keep or to sell as they wish.

On the face of it, the new Monsanto is quite different from the old one. In 2000, Hendrik Verfaillie, a company veteran, replaced Robert Shapiro as boss. Mr Verfaillie is seen as more pragmatic than the missionary Mr Shapiro, who preached the gospel of the “life sciences” and the synergies from mixing farming, food and pharmaceuticals. Not only has Monsanto lost its drug-making arm, but it has also shed its NutraSweet business. Within agriculture, it has narrowed its interest to four key crops—soyabeans, maize, wheat and cotton.

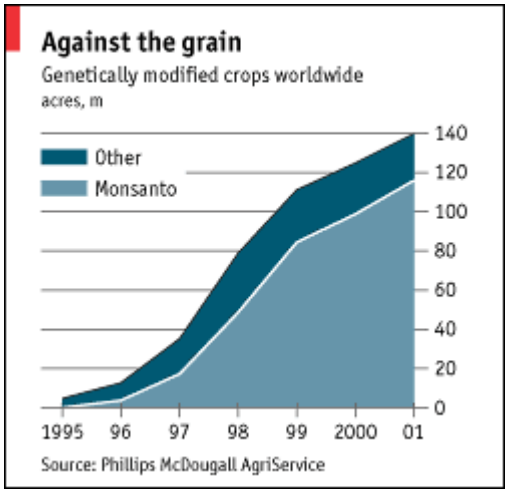
Hugh Grant, Monsanto's chief operating officer, says that Pharmacia gave the firm much-needed breathing space, assuming most of its debt and leaving it to get on with cutting costs and integrating the many seed companies that it bought in the late 1990s. The upshot is that Monsanto is now liquid once more. By the end of this year, it expects to have free cash flow of at least $400m.

Monsanto is not the only company in the industry having to tighten its belt. Rivals such as Syngenta and DuPont have also been cutting costs in order to meet profit-margin targets. This is particularly true in the crop-protection business: global sales of chemical pesticides are expected to shrink by more than 10% to $11.8 billion by 2004.

As John Moten of Deutsche Bank points out, the agrochemical and seed industry is under pressure on several fronts, including persistently low commodity prices and industry consolidation. The second of these has created bigger competitors in crop chemicals. Another factor is the economic meltdown in Argentina, a big consumer of chemicals. In the second quarter of this year, Monsanto wrote off $154m of unpaid bills there. Like its rivals, the company has since reduced its Argentinian risk by refusing credit and taking payment for goods only in cash or grain.

Although crop chemicals still account for almost 70% of Monsanto's revenues, their prospects are dimming, because the firm's bestselling herbicide, called Roundup, has gone off-patent. Monsanto sees its future in fancy seeds and genomics. Though it may not trumpet this article of faith quite as loudly as before, the firm is backing it with plenty of money: last year, 83% of Monsanto's $550m investment in research and development went into seeds and biotechnology, compared with an industry average of 29%. The latest crop of products close to being commercialised include GM maize, which resists a nasty pest called rootworm, herbicide-tolerant wheat and more nutritious feed for livestock.

European distaste



In Europe, where public resistance to GM foods has been fiercest, leading to a *de facto* moratorium on commercial planting of GM crops, betting on “Frankenstein foods” might sound like asking for trouble. But Mr Verfaillie points to the rapid adoption of GM crops outside Europe as farmers plump for the savings on chemicals that the use of such crops can bring (see chart). Mr Grant reckons that the environmental benefits of lower pesticide use and other ecological advantages—all hotly contested by anti-GM activists—should help to win over European consumers.

At the end of the 1990s, Monsanto made the mistake of assuming that brilliant science will speak for itself, and that public concerns are not worth worrying about. Mr Verfaillie admits that the company was arrogant and secretive in its dealings with the outside world, and blinded by its own technical success. This time round, the firm is big on public dialogue, talking to its customers, transparency and technology-sharing—all of which is embodied in an earnest promise (“The New Monsanto Pledge”) introduced by Mr Verfaillie two years ago. Mr Verfaillie is even mildly optimistic about the firm's long-term prospects in Europe. He is, after all, Belgian. That Monsanto is now talking to the public is good. But to win over the sceptics it will need to prove that it is listening as well.

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Serbia's Zastava

Yugo first

Aug 15th 2002
From The Economist print edition

Serbia hopes the sale of its only car maker will jump-start privatisation

IN THE 1980s, western car buyers knew Yugoslavia best as the exporter of the Yugo, a much derided communist-era clunker that shed its parts on roads across the United States and Europe. Jokes ridiculed the two-door hatchback, dubbed “the worst car of the millennium”. Zastava, which makes the Yugo, fared even worse than its product. During the Yugoslav war, western sanctions and heavy bombing brought the factory to a virtual standstill. Now the government wants to sell Zastava to a foreign car maker. It views the deal as a crucial test of its privatisation programme.

As ominous as that sounds, Zastava does have a few things going for it. It offers the last chance for a big car maker to gain a Central European brand on the cheap, now that Volkswagen owns Skoda of the Czech Republic and Renault has Dacia of Romania. Zastava will produce only 18,000 cars this year, but it has the capacity to make 200,000 annually—roughly the number it was producing in the late 1980s. It would thus give a buyer a foothold in the fast-expanding Balkan market.

AP

Versatile vehicle

What is more, Zastava's cars may be getting better. Starting in September, it will fit PSA Peugeot Citroën engines into its vehicles. Malcolm Bricklin, the man who brought the Yugo to America in the 1980s, wants to invest $100m-200m into exporting two-door, four-door and pick-up models to the United States.

Yugoslavia, which will soon be renamed Serbia and Montenegro, is committed to finding a foreign buyer for the business. The government, composed of westernised technocrats, has spent *euro*50m ($49m) on a restructuring of Zastava, which once made everything from hunting rifles to trucks. Some 27 unproductive units have been hived off, and the workforce has been reduced by two-thirds to 8,300. To lure buyers, the government says it would be willing temporarily to raise tariffs on imported cars.

Still, Zastava won't be an easy sell. Its brand is weaker than Skoda's. Global car firms are suffering from over-capacity and will thus be reluctant to invest the millions needed to upgrade the plant: Zastava cars do not meet western safety and emission standards.

A lot is riding on the sale, which the government hopes to close in the first quarter of 2003. Zastava not only provides a livelihood for its employees, but it indirectly supports 200,000 workers at local suppliers. The government thinks that selling the company will get the privatisation process going. Since the war ended in 1999, it has sold only some cement factories. Ivan Lujanovic, head of corporate restructuring at the Yugoslav privatisation agency, says a successful sale of Zastava will make it easier to privatise the 48 other state companies that urgently need to be restructured.

That may be wishful thinking. According to Chris Butters, head of PricewaterhouseCoopers in Belgrade, the current batch of firms for sale is not of the best quality. Many of the country's most profitable companies, such as its breweries, were sold cheaply to their employees in the early 1990s. Rather than make fresh acquisitions, says Mr Butters, foreign investors are more likely to form joint ventures, as Michelin has done with Tigar, a local tyre maker. Serbia may have buffed up Zastava, but once it is sold, the road for other privatisations will be downhill.

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Face value

Asia's Superman swoops again

Aug 15th 2002
From The Economist print edition

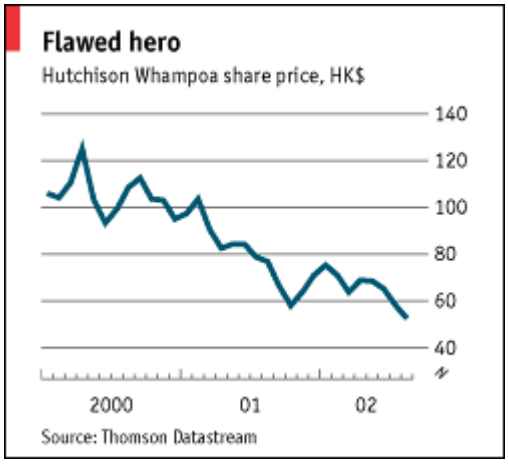
Is Li Ka-shing really the superhuman investor that Asians think he is?

IN ALL honesty, most of Asia's tycoons, no matter how illustrious they appear at home, are really keepers of glorified mom-and-pop stores. The main exception is Li Ka-shing. This is not because Mr Li dominates the economy of Hong Kong, where he runs most of the port (the world's biggest), has the monopoly on supplying electricity to the main island, ranks among the territory's top landlords and retailers, and owns the biggest mobile-phone operator. Rather, it is because he, alone in his region, regularly makes his powers felt all over the world, and even influences the future of whole industries.

At the moment, this is most evident in the telecoms industry. On August 9th, one of Mr Li's two main holding companies, Hutchison Whampoa, joined with a Singaporean partner to scoop up 61.5% of Global Crossing, a bankrupt American company with a global network of fibre-optic cables, for $250m. Inevitably, this invited comparisons between Asia's most famous investor and America's, Warren Buffett, who is also bottom-fishing for distressed telecoms assets.

Mr Li will make an even bigger impact this autumn, when Hutchison starts rolling out third-generation (3G) mobile-phone services in Britain, Italy, Sweden, Australia, Hong Kong, Israel and Austria. Europe's telecoms incumbents may be delaying their 3G launches, and investors may worry that the technology might flop, but Mr Li is undaunted.

This has produced two very different reactions. The markets—ie, mostly non-Asian fund managers—are punishing Mr Li for this gamble, and have marked Hutchison shares down by over half since early 2000 (see chart). On August 8th, Standard & Poor's, a credit-rating agency, said that it too was pessimistic about the outlook for Hutchison and its sister company, Cheung Kong.



Retail investors and the general population of Hong Kong, however, see it differently. In their minds, there is no question that Mr Li—whom they call *Chiu Yan*, or Superman—is infallible. When Mr Li launches a company, with or without a business plan, and lists its shares, they rush to buy—as they last did in July, when the initial public offering of Mr Li's life-sciences start-up was 120 times oversubscribed. If Superman now thinks that 3G is the future, why doubt it?

The people of Hong Kong remain wowed by Mr Li because, to them, he epitomises success, a mystique he is adept at cultivating. Hong Kong is a superstitious place, and it helps that Mr Li was born in 1928, an auspicious dragon year. His key buildings are blessed with excellent *feng shui*. He sets his watch eight minutes early, because “eight” sounds like “prosperity” in Cantonese. He regales his visitors with stories about his cheap watches to show what a simple, ascetic man he still is. He pouts self-pitifully (“Do you not want me to invest anymore?”) every time anyone dares to suggest that he is growing too powerful—and many do, all the more so now that Mr Li has said he wants a Hong Kong television network in addition to the local radio station he already owns.

Such controversies aside, does Mr Li deserve his reputation? In part, his success can be explained by

luck: he has been in the right place at the right time. From the 1980s to 1997, Hong Kong property was a one-way ticket to wealth, since the colonial government had a policy of restricting the supply of new land for building. Mr Li was among several developers who simply rose with land prices. Similarly, once he secured his niche in the container port, he piggy-backed on Hong Kong's rise as a trading hub. In 1997, when other Asian tycoons stumbled with their currencies, Hong Kong's dollar peg kept him standing.

Luck, however, is only part of it. Alone among Hong Kong's property tycoons, Mr Li knew when to branch out overseas and into new industries. Equally rare, he always found and hired the best professional managers, many of them foreigners. Most importantly, his investment record has, so far, outperformed that of all other Asian tycoons. Everyone who has worked with him raves about his nose for opportunity.

Like Mr Buffett, he appears to look for value, but comparisons with the Sage of Omaha are overdone. Mr Buffett crunches piles of numbers in the search for undervalued companies, then holds their shares indefinitely. Mr Li, by contrast, is, on the face of it, the archetypal Asian asset-trader. He tries to time the market. He is patient but swoops with phenomenal speed when opportunities present themselves. Global Crossing is a case in point. It has few synergies with Mr Li's other telecoms assets. Mr Li first made an offer in January, then withdrew it, and then came back with a new offer, two-thirds lower.

More than just a trader

Yet even the label “asset-trader”, appropriate for most Asian tycoons, appears too small to fit Mr Li. Transactions have made him famous—his biggest coup was the perfectly timed sale in November 1999 of his stake in Orange, a British mobile-phone operator, for a profit of around $15 billion. But he also knows how to build a business. In Orange's case, he had nursed it for years before the sale. That skill, Mr Li's fans reckon, should ensure that he will be able to turn 3G into a winning proposition.

Clearly, Mr Li ought never to be underestimated. On the other hand, his record has blemishes, though few remember them. In the 1980s, he invested in a Canadian oil company that went on to underperform for years. Even in mobile telephony, his first venture in Britain, called Rabbit, flopped. Ultimately, the best way to analyse Mr Li may be to compare him with celebrity fund managers who, for whatever reasons, outperform for some time, then use their fame to play with ever bigger sums and, sooner or later, start underperforming just like everybody else.

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Monetary policy in the United States

A double dip?

Aug 15th 2002
From The Economist print edition

Hulton

The next move in American interest rates will probably be down

THE British government has just announced that the queen is to bestow on Alan Greenspan, chairman of America's Federal Reserve, an honorary knighthood for his contribution to global economic stability. Knights used merely to have to slay the odd dragon. In comparison, Mr Greenspan's task of preventing another recession, or even deflation, looks trickier.

The Federal Reserve is not yet convinced that America's economy is heading for a double-dip recession. At its policy meeting on August 13th, the central bank decided to keep its federal-funds rate unchanged, at a 40-year low of 1.75%. Still, it signalled a readiness to cut rates should the economy look like weakening further.

Earlier this year most economists had expected the Fed to raise interest rates during 2002. Now many predict that rates will be cut before the year is out. In the past few weeks the recovery has started to look shaky. For a start, GDP growth in the second quarter slowed to only 1.1% at an annual rate. In July, the purchasing managers' indices of activity in both manufacturing and services fell sharply; total hours worked also declined. Retail sales rose by a robust 1.2% in July, yet this was due mainly to car firms offering interest-free loans. Not counting cars and petrol, retail sales were flat. Ominously, consumer confidence fell sharply.

The slide in confidence partly reflects the slump in equities. Share prices have picked up a little from their late-July lows, yet America's stockmarket is still worth about $7 trillion less than at its peak in early 2000. The loss has partly been offset by a rise in house prices, but the latest figures suggest that the housing market may now be cooling. For the third year in a row, households are likely to see their net wealth shrink. Savings rates are still historically low, so unless share prices rebound, households will probably have to start saving more and spending less.

Another cause for concern is tighter conditions for corporate credit. Not only have banks tightened their lending standards; borrowing in the corporate-bond market has also got much tougher. Interest-rate spreads (the difference between the yield on corporate and Treasury bonds) have widened sharply. As a result, many firms face a higher cost of capital, despite the fall in the yields on government bonds. A crunch caused by firms finding it hard to refinance their debts would trigger a second round of cost cutting.

These are all reasons to expect the Federal Reserve to cut rates again, possibly at its next meeting on September 24th. Perhaps the strongest reason, though, is that if the economy does slip back into recession, it will be at a point of very low inflation. America's GDP deflator rose by just 1% in the year to the second quarter. Another slump in output would nudge the economy dangerously close to deflation.

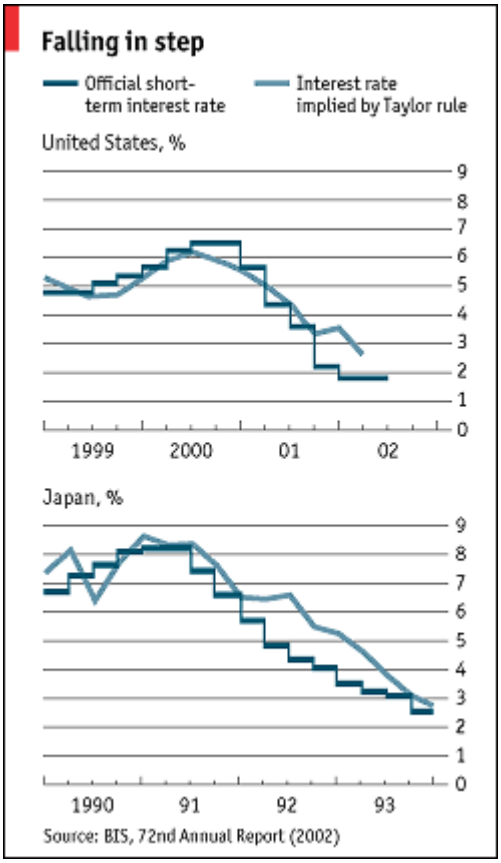
Japanese lessons

A recent study* of Japan's slide into deflation, by economists at the Fed, suggests that Mr Greenspan is well aware of the risks. The study concludes that monetary policy was not too tight in Japan in the early 1990s, given the outlook at the time for growth and inflation. Indeed, the authors calculate, interest rates were generally lower than warranted by the so-called Taylor rule. Named after John Taylor, now at America's Treasury Department, the rule is a popular method for calculating the appropriate interest rate on the basis of inflation rates and the size of the output gap. The snag is that forecasts for growth and inflation consistently proved too high. Few, in Japan or abroad, forecast deflation at the time—including economists at the Fed.

Once the price level started to fall in 1995, it was much more difficult for monetary policy to spur the economy. Interest rates cannot go below zero, so if inflation is negative, real interest rates become too high. The authors describe the failure to forecast deflation in Japan as “a cautionary note for other policy makers in similar circumstances”. They conclude that, when interest rates and inflation move closer to zero, and there is a risk of deflation, central banks need to cut interest rates more forcefully than is normally justified by forecasts of inflation and growth.

The popular perception is that the Fed did indeed cut interest rates last year more aggressively than did the Bank of Japan in the early 1990s. However, when looking at what the Taylor rule would have prescribed, an analysis in the latest annual report of the Bank for International Settlements (BIS) finds little difference between the speed with which the Bank of Japan responded to its downturn in the early 1990s and the Fed's response last year (see chart).

The Fed study gives Mr Greenspan justification for further rate cuts. Yet not everybody agrees with its conclusions. Robert Feldman, an economist with Morgan Stanley in Tokyo, argues that the Fed may be drawing the wrong lessons from Japan.



The Taylor rule ignores how the level of potential output, and hence the output gap, can be affected by monetary policy. One lesson from Japan, Mr Feldman says, is that interest rates at or close to zero keep inefficient firms in business; and the persistence of excess capacity may then worsen deflation. The BIS raises the same concern, but adds that the argument may carry less weight if other mechanisms, such as active bankruptcy courts and vigilant bankers, ensure that untenable firms are restructured or closed down. Part of Japan's problem is that banks continue to roll over bad loans rather than write them off and force unprofitable firms to close. In America's more flexible and competitive economy there ought to be fewer obstacles to destroying capacity.

Despite this, Mr Feldman worries that further monetary easing in America might help delay a necessary, yet painful, purging of excesses from the bubble years. Personal saving is still far too low, and corporate and household debt far too high. Excess capacity still needs to be cut. Recessions have a corrective effect. Yet even after recent, downward revisions to GDP, last year's recession was still one of the mildest on record—too mild to do much about the excesses.

Here lies the Fed's dilemma. Lower interest rates may now be vital to lessen the deflationary risks, including the risk that deflation would further increase the debt burden of households and companies. Yet easy money has encouraged people to borrow more and has thus delayed the inevitable adjustment in households' balance sheets. The role of monetary policy is to ease such adjustments, not to postpone them. As a result, an overhang of debt could act as a drag on growth for several years to come.

Most American economists weigh up America's prospects as if there were only two options: a double-dip recession, or a sustained recovery. A third and possibly more likely option is a protracted period of growth well below trend, until America had shed its excesses.

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* “Preventing Deflation: Lessons from Japan's Experience in the 1990s”. International Finance Discussion Papers No. 729, June 2002.

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Brazil and the IMF

A matter of faith

Aug 15th 2002 | SAO PAULO
From The Economist print edition

Will a big bail-out led by the IMF allow Brazil to avoid defaulting?

AP

Helping the optimal equilibrium along

THE financial markets' euphoria over Brazil's $30 billion rescue by the International Monetary Fund, announced last week, was short-lived. The *real* soon fell back below three to the dollar, and the risk premium on Brazil's government bonds rose. President Fernando Henrique Cardoso called meetings, for August 19th, with the four main candidates to succeed him in October's election, to plead with them to commit themselves to the Fund's conditions and thus calm the markets. Though the two leftish contenders who lead the polls, Luiz Inacio Lula da Silva and Ciro Gomes, no longer talk of "renegotiating" Brazil's debts, investors worry that the country may be unable to repay them, even with the Fund's help.

The IMF package aims to boost Brazil's reserves sufficiently to ward off any further speculative attacks against the *real*, and to finance its big current-account deficits for this year and next. The point is to reassure lenders sufficiently for them to want to resume lending to Brazil's government and companies at reasonable rates, dissipating any talk of default. The optimists, led by Pedro Malan, the finance minister, point out that the package is bigger than the markets had hoped for, and thus bound to succeed. There are also doubters. Moody's, a credit-rating agency, this week downgraded Brazil to five notches below "investment grade", fearing that the next president—whoever wins—may be unable to meet the Fund's demands, such as raising the current target of a 3.75% surplus on the primary budget (that is, before interest payments) if this is needed to stabilise the public debt.

Both the upbeat and the downbeat point to precedents. Brazil last defaulted on its debts only 15 years ago; Argentina did so eight months ago, despite lashings of IMF cash. On the other hand, Brazil defied predictions of default after its forced devaluation in 1999. This week's wobbles do not prove that the new bail-out is doomed: J.P. Morgan Chase, an investment bank, notes that turbulence continued for weeks after the announcement of other rescues that in the end succeeded, such as Mexico's in 1995 and South Korea's in 1997.

So who is right? A new paper* on Brazil's debt sustainability, by John Williamson of the Institute for International Economics in Washington, DC, concludes that, even with the new bail-out, things could go either way. Until the 1980s, he explains, economists took the deterministic view that any set of starting conditions had but one probable outcome. More recently, a theory of "multiple equilibria" has gained support, in which there is more than one probable outcome, with market expectations usually the deciding factor. Brazil's total public debt, or its foreign debt, both public and private, could either be sustainable or could become unmanageably large, depending on what the markets henceforth expect.

Mr Williamson starts by asking: how much debt? This is no simple matter. For instance, it is hard to know which government assets and liabilities (eg, those of state-owned banks) should be counted towards its net indebtedness. And the oscillations of the *real* make it hard to put a value on the chunk of debt tied to the dollar. Mr Williamson reckons that Brazil's net public debt on August 8th, the day after the IMF announced its rescue, was 841 billion *reais*, or $288 billion at that day's exchange rate—that is, equivalent to two-thirds of Brazilian GDP, up from 30% in 1994.

As for the foreign debt, the government has $56 billion, net of its reserves, while Brazilian firms' gross external debts are estimated at $120 billion. Though Brazilian companies and individuals have big foreign

assets (estimates range from $70 billion to $170 billion), many of these are illiquid (eg, factories) and those that are liquid (eg, offshore bank accounts) would not be repatriated in an emergency: on the contrary, more Brazilians have been sending money offshore. So Mr Williamson puts the effective foreign debt at an alarming $176 billion. Brazil is already having to commit nine-tenths of its currency earnings from exports to servicing foreign debt and to financing the remittances of foreign firms' Brazilian operations.

Nevertheless, if the markets now become convinced that a default can be avoided, the *real* should recover some of its recent losses, lenders should resume offering money at reasonable rates of interest, and Brazil should resume reasonable growth, of around 4%, say. This would be enough, Mr Williamson reckons, for the public debt-GDP ratio to start falling, and for fears to be eased that Brazil is running out of dollars to pay its foreign debt. But if current market conditions continue, disaster looms: if the *real* does not recover, and Brazil has to roll over its expiring debt at current market rates, then the debt-GDP ratio could rise by another nine points this year. That, says Mr Williamson, is scary. Three-quarters of the government's debt is with local investors, who can be leaned on to keep funding it. Yet the debt ratio could reach a point where it becomes politically impossible to cut spending and raise taxes any further to try to stabilise it.

Nervous foreign banks are reeling in their credit lines to Brazilian firms, forcing these to buy dollars to repay their expiring loans, sending the *real* down further and so increasing the chances of an eventual default. In Brazil's crisis of 1998-99, Bill Clinton's administration leaned on American banks to roll over Brazilian debts and avoid a crunch. Mr Williamson suspects that George Bush may be less inclined to do this. Brazil's central bank has agreed with the IMF to use some of the country's reserves to lend to companies in difficulties. But a second default trigger, set off by a shortage of dollars, remains possible.

Other economists have reached conclusions similar to Mr Williamson's: investors themselves will decide whether Brazil will default on the money it owes them. They may be swayed either way by the responsibility, or otherwise, that Brazil's politicians now show, in the light of its grave situation. A few well-chosen words, or even—miraculously—some deeds, such as approving much-delayed tax reforms, might avert a disaster.

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* "Is Brazil Next?", by John Williamson. Institute for International Economics.

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About sponsorship

Japanese banks and their interest-rate swaps

Free lunch, for now

Aug 15th 2002 | TOKYO
From The Economist print edition

Swaps make a disturbingly handy source of income

Get article background

WHEN profits are hard to come by, accounting loopholes make nice sources of income. Japanese banks, which need to offset huge losses from write-offs of bad loans, have managed to raise revenues by exploiting a loophole allowing them to pile up big exposures to derivatives, without having to disclose them to investors.

Banks make money through speculative purchases of interest-rate swaps, locking in income from a fixed rate of interest in return for paying a lower, floating rate. In a recent report, Standard & Poor's, a credit-rating agency, calculated that income from interest-rate swap transactions supplied 80% of the unexpected increase in revenues at Japan's second largest bank, Sumitomo Mitsui Banking Corporation (SMBC), in the year to March 2002.

Banks are thought to have stocked up on some ¥40 trillion ($342 billion) of interest-rate swaps, roughly the same as their holdings of government bonds. They have, in other words, quietly doubled their exposure to interest-rate fluctuations. Some, such as SMBC and UFJ Bank, one of the few banks thought to have neutralised its exposure, now disclose their swap figures. The remainder keep positions under wraps, making it hard to tell how much they own, or what proportion is in riskier, longer-dated maturities. Some estimates suggest that, thanks to banks' swaps holdings, a rise of one percentage point in long-term interest rates would wipe more than ¥3 trillion from banks' capital, equivalent to a year's worth of operating profits.

The spread between swap rates and the yields on government bonds backs this up. Since governments are considered to be less risky than private institutions, government-bond yields ought by rights to be lower. Yet over the past year, and thanks to great demand from banks, the rates on swaps with maturities between five and 15 years have fallen and are now a good deal lower than the yields on government bonds. With sweet justice, some think, the many foreign hedge funds that acted as banks' counterparties have borne the losses, forcing some to quit Japan.

The accounting loophole has been closed in other rich-world jurisdictions. In Japan, it has been kept open once already, but is now meant to be closed next April. Japan's Institute of Certified Public Accountants insists that the deadline will not be moved again—bar an emergency, of course, such as the risk of a financial crisis.

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About sponsorship

Banks in search of a strategy

Displacement activity

Aug 15th 2002
From The Economist print edition

European banks look across the Atlantic, when they should look to their backyard

FEW signals from the world's top bankers these days inspire any confidence that they know where they are going. Sandy Weill, head of Citigroup, the world's biggest financial conglomerate, found himself last week as good as apologising for being in the banking business and undertaking, on behalf of his troops, to deal only with firms that share the bank's supposedly open values. The lame-duck head of Credit Suisse, Lukas Mühlemann, this week promised he would turn round Winterthur, the group's troubled insurer, without spelling out how that is possible when equity markets are depressed. Even at Lloyds TSB, a British retail bank which has made a virtue of sticking to its knitting, the chief executive, Peter Ellwood, hinted earlier this month that overseas expansion is an option, yet offered no indication of where and when.

These banks, and most of their peers, give the impression of being caught in the headlights. When markets are uncertain, profits are down, and their share prices have fallen, banks have few options. For several badly performing banks—including Germany's Commerzbank and ABN Amro of the Netherlands—the obvious option is to be broken up or sold. Allianz, Germany's biggest insurer, ought to sell much of Dresdner Bank (see article), as Credit Suisse should Winterthur. Certainly, weak stockmarkets help prevent the sensible from happening. But so does a mixture of national pride, doggedness and denial among executives and owners.

Potential predators, such as Citigroup, Bank of America, UBS, Switzerland's biggest bank, and Deutsche Bank, Germany's biggest, are afraid to act, because their share price is either low already, or would “crater”, as one former chief executive puts it. Josef Ackermann, head of Deutsche Bank, has promised no big acquisitions for the time being. UBS, on the other hand, although a reluctant acquirer at the moment, may one day find that the Swiss regulators hand it a weakened Credit Suisse.

Executives at many banks may argue that their options are limited by shareholders bent on quarter-by-quarter outperformance. If it were not for that, they would do what Royal Bank of Scotland has done in America. It bought a small east-coast bank 15 years ago and added to it, piece by piece, so that it now has a regional presence that is as much American as British. Or what ABN Amro has done around Chicago, where it has a cluster of retail and corporate banks that generate nearly half of the group's worldwide profits.

Shareholders may approve of expansion, yet they demand a return on equity. Expanding a bank, however, in a way that increases equity returns in the long run, needs a 15-year horizon, not one of three months or even three years. Hence a dilemma for chief executives.

Britain's biggest bank by far, HSBC, with oodles of deposits in Asia, Britain and America, has had the luxury of time, size and market capitalisation to buy abroad small- and medium-sized banks with potential, in a way that hardly dents its balance sheet. This way, it has picked up Republic National Bank in New York and Switzerland, CCF in France and even Demirbank in Turkey.

Now rumours are growing that the two other big British banks, Lloyds TSB and Barclays, are looking for acquisitions in America. FleetBoston Financial has been mentioned as a vulnerable target, because of its losses in Argentina and in an investment-banking subsidiary. The banks should be careful. America is the graveyard of many European banks' ambitions. In 1980, Midland Bank bought Crocker National Bank in California, only to find it riddled with bad corporate and emerging-market loans. That fatal mistake eventually drove Midland into the arms of HSBC. American ambitions were the ruin of S.G. Warburg, a British merchant bank, and probably also of National Westminster, which is now part of Royal Bank of Scotland. The latest cautionary tale is that of Allied Irish Banks, whose subsidiary Allfirst, in Baltimore,

lost $690m thanks to a rogue trader. In appraising the benefits of mergers, long-distance managers usually fail to factor in the risk of accidents.

Beside the point

Why look to America, a mature market where even the British have little comparative advantage? To some extent it is all displacement activity, in the psychiatrist's jargon, since the alternative—Europe—is a bank-buyer's nightmare. Yet banking consolidation in Europe is the real issue.

Those exhibiting paralysis fail to foresee the inevitable consolidation that will accompany a single European market in financial services. Otherwise, they would be launching hostile bids, or engineering break-ups in cases where the whole is worth less than the sum of the parts. ABN Amro is a case in point. It has three regional business clusters—in Brazil, the Netherlands and the United States—which bear little or no relation to each other. Until 1998, ABN Amro aimed for the top, wanting to compete with Citicorp (as Citigroup then was) and J.P. Morgan in global universal banking. No longer. Credit Suisse has spent its resources taking on America's “bulge bracket” of investment banks, like Goldman Sachs and Morgan Stanley. It is still, by its own reckoning, a market leader in mergers and acquisitions and high-yield debt, but at what cost?

All the more need to return to Europe—where, after all, some of the perceived barriers are more political than economic. For instance, the French and Italian governments continue to resist foreign ownership of their national champions. Elsewhere, a proposed marriage of Deutsche Bank and Lloyds TSB apparently foundered because of a disagreement over where a merged group's headquarters should be.

Maybe it needs a shock, like the sudden weakening of a desirable target bank, to get consolidation in Europe going. Or perhaps some brave chief executive will take his eye off the share price for a moment and steer for the horizon 15 years away.

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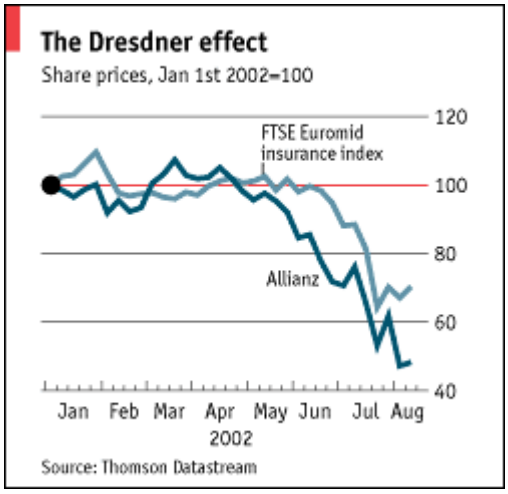
About sponsorship

Allianz and Dresdner Bank

For better, for worse

Aug 15th 2002 | FRANKFURT
From The Economist print edition

Should Allianz rue its purchase of Dresdner Bank?



HOW happy the couple were on that sunny April morning last year, when the banns were read to a packed congregation of journalists. Dresdner Bank, Germany's third-largest bank, at last had a partner after two failed romances. Allianz, Europe's biggest insurer, had got not only a sales channel for its life policies, but also a good-sized asset manager, Dresdner's DIT. It would be a thoroughly modern marriage, perfect for Germany's evolving retail financial market.

A year after the actual wedding, not all is bliss. Dresdner, never a great beauty, now looks hideous, having lost over *euro*1 billion ($980m) in the first six months of 2002, prompting a profit warning from Allianz at the end of July. Apart from the bank, said Allianz in its first-half results on August 14th, business is not at all bad, considering these jittery times. Admittedly, falling stockmarkets have forced Allianz to write down its portfolio by almost *euro*2 billion. Yet it is winning market share as Germans shun smaller insurers for the safety of a big name.

In the past year almost one-fifth of Dresdner's revenues have crumbled away. The trouble lies in Dresdner's “corporates and markets” division, which includes Dresdner Kleinwort Wasserstein, its investment bank. As equity markets have weakened and mergers-and-acquisitions business has dried up, trading revenues have fallen by more than half, and fees and commissions have dropped by more than one-eighth.

Dresdner has cut costs hard—by 14% in a year, no less—but not yet by enough. Its cost-income ratio has soared to 99%. Then there are bad debts, ratcheted up by a series of big German bankruptcies, including that of Kirch, a big media company, and by the turmoil in Latin America. Dresdner has almost doubled its bad-loan provisions in the past year, to a hefty *euro*1.1 billion. Ten borrowers clocked up *euro*370m between them.

In response, Allianz plans to cut Dresdner's costs by a further *euro*700m a year (about 10% of the current total) before the end of 2003. Dresdner's loans in the Americas and Asia, where it once had grand ambitions but which it is now quitting, will be put into a separate business unit, along with loans, private-equity investments and other Allianz assets unlikely to pay their way. Dresdner's corporate centre in Frankfurt will see some functions passed down to the bank's two divisions, while others will go to Allianz's headquarters in Munich.

A failed merger, then? Not at all, says Allianz. The logic behind the deal was always in the retail market. The problems in Dresdner's corporate division are real enough, and must be put right. But the bank's retail side, Allianz insists, is doing fine. Why, it even made a profit in the first half of the year. Granted, it was only *euro*28m, and these are still early days, but the integration of the bank and the insurer has begun pretty well. Some 860 insurance sellers now work in bank branches, and sales of insurance policies through this channel have quadrupled in the past year. The strengthened link with Dresdner has more than made up for the ending of an arrangement with HypoVereinsbank (HVB), Germany's second-biggest bank. Insurance offices in which some 110 bank advisers are working have so far pulled an extra *euro*250m into investment funds. About 200 such advisers will be in place by the end of the year.

On top of this, Allianz points to another market-realigning deal—made possible by the Dresdner

takeover—with Munich Re, another big insurer. The two insurers are neighbours in the same Munich street, and own about one-fifth of each other's shares. When Allianz bought Dresdner Bank (of which it already owned more than one-fifth) it handed 13.6% of HVB to Munich Re in exchange for 40% of Allianz Lebensversicherung, a life insurer of which Allianz already owned just over half. Since then, HVB's shares have fallen by two-thirds. Allianz Lebensversicherung's new business rose 29% in the first half, compared with a market average of 13%.

Success is far from sealed, though: bankers and insurers have long lived happily under the same roof in France and Spain, and more recently in Belgium and the Netherlands, but have had less joy together elsewhere. And even if Allianz makes a go of *bancassurance* in Germany, the merger could yet be judged a mistake if the benefits are outweighed by losses at Dresdner's corporate wing. After all, Allianz bought the lot.

Given the retail logic of the merger, there is no compelling reason to hold on to the corporate division for ever. One day it could be floated, or—given its focus on Germany and Britain—paired with a French or Italian bank. Sold or kept, though, the division will be worth more in profit. Its cost-cutting programme is two-thirds done. The generous guaranteed bonuses handed out in recent years to retain investment bankers have almost run their course; from next year, pay will depend on performance. And then Dresdner will have to start putting money into Allianz's pot.

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Economics focus

The fruits of fieldwork

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Might visiting a pin factory provide insights official statistics cannot?

ECONOMISTS, the worldly philosophers, do not on the whole live up to that tag. They are familiar enough with the economy as it exists in equations and official statistics, but are fair strangers to the economy as it exists behind cash tills and on assembly lines. It was not always so. Adam Smith opens “The Wealth of Nations” with a finely observed account of a visit to a pin factory, from which he goes on to demonstrate the benefits of the division of labour.

Surprisingly few economists visit the pin factories of today. An exception is Alan Blinder of Princeton University. For his 1998 book, “Asking About Prices”, Mr Blinder and his graduate students visited 200 American companies, to find out why managers are slow to raise and lower prices. America's National Bureau of Economic Research (NBER) went a step further. It launched its own “pin-factory initiative”, dispatching scores of economists to car makers, razorblade manufacturers and gene splicers, in a hunt for the source of America's productivity growth. Even so, most economists still consider fieldwork—“learning by asking”, as Mr Blinder puts it—a doubtful activity, one reserved for the lowest orders, such as reporters and sociologists.

Should economists get out more? The desk-bound point to over 10m business establishments in America: what can a handful of visits tell you about the economy as a whole? Statistical research has rigorous, agreed-upon standards for generating a sample and inferring beyond it. Fieldwork, they aver, does not.

Neither objection is fatal. Visiting can be just as rigorous as counting. After all, data is just the plural of anecdote—as long as the anecdotes are scrupulously and systematically chosen.

Nor can the official statistics measure everything that economists consider important. Mr Blinder wanted to know why prices are less flexible than they theoretically should be. Yet no government bureau compiles statistics on what prices should be, only on what they are.

The official statistics are not much better at measuring productivity. Back in 1987, the year he became a Nobel laureate, Robert Solow complained of a “productivity paradox”: the computer age was to be seen everywhere except in the productivity statistics. By the late 1990s, the statistics finally seemed to get it, apparently confirming a productivity miracle thanks to information technology. Since then, however, downward revisions have put the miracle in doubt. Paradox, miracle, or mirage? Little wonder some economists want to go out and check for themselves.

Learning by asking

Can managers in the field explain what the data cannot? Another Nobel prizewinner, Milton Friedman, has long doubted it. For Mr Friedman, economic behaviour owes as much to “market selection” as it does to express intention. Firms maximise profits because, if they did not, they would no longer be in business. Thus a firm's managers may be successful without being very good at explaining the principles underlying their success. A successful manager, in Mr Friedman's eyes, is like an expert billiard player. He can make the cue ball do his bidding, but he cannot explain the physics behind a cannon or a kiss.

So did Mr Blinder or the pin-factory economists learn anything new? After hundreds of interviews, Mr Blinder was still unable to declare an outright winner among the competing theories of inflexible prices—though he did narrow the field somewhat. Some of his interviewees were only too reminiscent of Mr

Friedman's billiard player, failing to grasp fundamental concepts like the difference between average costs (the cost per unit produced) and marginal costs (the additional cost of producing one more unit).

The NBER team also failed to pinpoint the source of the rise in American productivity in the 1990s. At the Ford car plant in Ohio, for example, productivity gains came from simple automation, replacing men with machines. At Toyota's plant in Kentucky, gains came from ergonomics, fitting the machine to the man. One of the more striking impressions was also faintly ironic. Much of the new economy, Robert Gordon of Northwestern University observed, takes place in front of computer screens, in workplaces indistinguishable from the university offices he and his colleagues had escaped from.

Still, the economists all felt better for their day out. Edward Lazear of Stanford University was glad of his visit to Safelite Auto Glass. The company's switch from time-rates of pay to piece-rates gave Mr Lazear tangible examples of the link between pay and motivation, examples that stuck in readers' minds long after they had forgotten his statistics. It is, he says, one of his most-cited papers.

Maybe these visits are not so different from Adam Smith's. As it happened, he did not discover the division of labour at his pin factory: the concept was already understood by his teacher, Francis Hutcheson. Even his painstaking description of the “18 distinct operations” of pin making was probably cribbed from Diderot's encyclopedia. In short, Smith might well have written his famous passage from his ivory tower at Glasgow University. Yet, as Mr Lazear discovered, even if fieldwork fails to inspire a hypothesis or prove a truth, it can help to sell ideas. The pin factory certainly helped Adam Smith rack up a few citations over the years.

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About sponsorship

Surveillance

Something to watch over you

Aug 15th 2002
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GlobeXplorer

WorldSat International/Earth Satellite Corporation/Digital Globe/NOAA

It is easier than ever for individuals to track their possessions, pets and loved ones

HILLARY CLINTON is supposed to have said of her husband that he was a “hard dog to keep on the porch”. She is not alone. All over the world, dogs, husbands, children and even inanimate objects are liable to stray from the home—whether willingly or otherwise. Now, though, the technology exists to keep track of them.

In fact, the new generation of tracking devices combines two existing technologies. One is a global-positioning-system (GPS) chip, which uses radio signals from a network of satellites to work out where it is on the earth's surface to within a few metres. The other is a mobile-telephone chip, which broadcasts that location to whoever needs to know it. The result is a pocket-sized, or even wrist-sized, personal locator.

Track to the future

Applied Digital Solutions (ADS), of Palm Beach, Florida, calls its version of the technology a “digital angel”. The angel comes in two versions. People get a pager-like device that clips on to their clothing. Animals get a collar.

The angel is intended to look after old people who have become forgetful and young children who have become too adventurous, as well as dogs who are too interested in the bitch next door. The wearer's guardians define a perimeter beyond which they feel their charge should not wander, and receive alerts via mobile phone or pager when he has gone beyond these boundaries.

The digital angel can also issue an alert when its wearer has fallen down, or when there has been an unexpected change in local temperature of the sort that might be caused, say, by someone falling into a pond. For that to happen, the wearer needs to sport a specially modified wristwatch which has suitable sensors and a wireless link to the pager. Moreover, ADS claims to be on the verge of introducing a version of the watch that can collect and broadcast medical data such as pulse rate, blood pressure, body temperature, electrocardiogram readings and even blood chemistry.

More intrusive devices will soon be available. Next month Wherify, of Redwood Shores, California, plans to start selling a lockable bracelet designed, it says, for children up to the age of 12. This will allow a child's parents to use the web to see a recent satellite photograph of their offspring's location. Parents will also be able to track their child's recent movements, and set up an alert system so that they will know if he does not turn up somewhere he is expected. Expect trouble, though, if you try to insist that

your privacy-loving teenager wears one.

For those who like their technology to be a little more integrated and invisible, there is now the prospect that parts of tracking devices could be implanted in the body. Indeed, ADS already produces a device the size of a grain of rice that can be inserted beneath the skin, and nine volunteers are trying it out.

ADS's device is a type of radio-frequency identification (RFID) chip. Such chips are already implanted into animals to act as “pet passports”, identifying beasts that do not need to go into quarantine when they cross frontiers. When an RFID chip is “interrogated” by a reading machine operating at the right radio frequency, its antenna picks up a small amount of energy from the signal. This is used to power the chip. The device then broadcasts data in the chip back to the reader.

At present, ADS's chip does not store anything more than a unique identification code. That has limited applications (though it could, for example, allow a bank's cash machine to identify someone without their needing to type in an identification number). The code in an RFID chip can, however, be used to refer to medical data that might be required in an emergency, and in the future such chips will have the potential to hold such data in their own right.

They could also cope with other sorts of emergency. They could, for example, be linked wirelessly with digital angel units so that if the connection between unit and chip were broken (for example during a kidnapping, when the digital angel was discovered and removed), then an alert would be issued. This may not prove necessary, however. In response to “enormous customer demand”, ADS is accelerating development of a GPS-based personal location device that could be fitted entirely under the skin. The device would be powered by the sort of battery used in heart pacemakers, and the company says a working prototype is expected within seven months.

Tracking technology also has applications when a criminal has been caught. At the moment, some convicts are sentenced to a form of house arrest that relies on their wearing an electronic tag. Such tags, though, are crude devices that are linked by radio with a base station attached to a telephone. If the tag moves too far from the base station, a call goes to the authorities saying their prisoner has absconded.

New-style tracking allows a more sophisticated approach. Pro Tech Monitoring, of Tampa, Florida, makes a system that tracks people on parole and probation. In a sense it works in the opposite way to a digital angel—alerting the authorities if it enters a designated exclusion zone such as a school or a previous victim's house, rather than if it leaves a permitted area (though it may do that, too, in order to keep someone within a particular jurisdiction). This allows a parolee or probationer to live a more or less normal life. It can also give victims of crime, or witnesses, a warning if a perpetrator is nearby. In theory such systems could even be used to tell how fast someone was driving.

Tracking technology may even help to solve crimes, as well as preventing and punishing them. Wherify is looking into the possibility of making a flat version of its tracking device that could be slipped into a stack of banknotes. Such marked stacks could then be handed over to bank robbers, who would find that their haul included rather more than they had bargained for.

Eventually, this kind of technology will almost certainly be miniaturised to the point where it can be sewn into belts, shoes or clothing. It should also become cheaper (at the moment, individual devices cost several hundred dollars each, plus a monthly subscription fee). This could mean that people would be able to use lots of these devices, tracking many aspects of their environment. Hide and seek will never be the same again.

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Quantum computers

Trapping the light fantastic

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Lasers and lenses give a new sort of quantum computer a big leg-up

Get article background

QUANTUM mechanics, the theory that explains how the universe's fundamental particles behave, thrives on reconciling opposites. According to its topsy-turvy tenets, it is perfectly all right for a particle to smear away into space like a ray of light, while a beam of light behaves like a collection of tiny, distinct particles. So it is fitting that an idea about quantum mechanics itself that once seemed far-fetched may soon appear just the reverse: it now looks possible that scientists may some day harness quantum principles to build a computer.

A quantum computer could solve problems that a conventional computer could never manage, such as factoring enormous numbers for code breakers or simulating the intricacies of complicated systems. This is because such computers would rely on quantum bits (qubits) to store and process data. Unlike conventional bits (the ones and zeros of the binary arithmetic that existing computers employ), qubits can be in two states at once. Because each qubit can simultaneously process a zero and a one, a quantum computer could zip through lots of calculations in parallel. A regular computer, in contrast, has to carry out each calculation in turn.

Manufacturing devices that can store qubits is therefore the most important part of making a quantum computer. It is also proving the most challenging. The best efforts to date have produced seven- or eight-qubit systems—a considerable accomplishment, but far from the number required for solving any interesting problems. Now, a new technique may bring some of those problems within reach. Physicists working at the University of Hanover's Institute for Quantum Optics think they have worked out a way to make qubits that would beat the previous record by a factor of ten.

Wolfgang Ertmer, Gerhard Birkl and their colleagues plan to use rubidium atoms as their storage devices. A lone rubidium atom can exist in one of two different low-energy quantum states, meaning that it can act as a qubit store. But holding enough lone rubidium atoms in place to have a chance of making a working computer is tricky. Going on to read them so that the values of their qubits can be known is doubly so.

As the researchers report in a forthcoming issue of *Physical Review Letters*, they managed to hold significant numbers of isolated rubidium atoms in place by shining a laser beam on to an array of microscopic lenses. Light passing through each microlens focuses at a point a few tenths of a millimetre beyond it, and thereafter spreads out as a cone. This conical beam is then reflected into a cluster of 1m or so rubidium atoms, which are held trapped in a magnetic field within a vacuum chamber.

One effect of the beam is to polarise the cloud of electrons surrounding each rubidium nucleus, meaning that part of the atom becomes a negatively charged pole, and part a positively charged pole. The result is that the atoms interact with the beam, are drawn into it, and settle at the tip of the cone—a phenomenon known as dipole trapping.

Using this technique, and a sufficient number of microlenses, the team created an array of 80 dipole traps, each of which captured about 100 rubidium atoms, spaced 125 microns from one another. With sufficient cooling, Dr Birkl reckons, these traps could be made to hold on to just one atom each, thereby producing 80 individual qubits.

One advantage of this method of making a quantum computer is that the atomic qubit stores can be manipulated relatively easily. Using pulses of laser light aimed through the appropriate microlenses, the

researchers were able to set each of the qubits into a particular initial state—a necessary precursor to any calculation. Another advantage is that when the atoms are left alone, they do not change state too quickly. That means they are likely to prove sufficiently sturdy to perform quantum computations.

Doing actual calculations with these trapped atoms will be hard, because the qubit stores must interact with each other during the process. The researchers plan to solve this problem by using two laser beams focused through the same array of microlenses. By placing the beams at a slight angle to each other, they are able to create an interleaved set of dipole traps. These can be made to overlap with each other by altering the angles of the beams. This means that atoms in different traps could be brought together, made to perform a computation and then separated. Then the result of the computation could be “read” by laser once the qubits were comfortably sequestered again.

At the moment, the researchers are at the beginning of this process. It will be a long time before they are putting any conventional computer makers out of business. But their demonstration of dipole trapping at least shines a captivating light down the path to quantum computing becoming a practical technology.

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Human evolution

The long and the short of it

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Short women have more children than tall ones

THAT tall men have more sexual partners and more children than their shorter brethren is well known. The reason is that height in men is attractive to women. But it is a comment on who the authors of such studies usually are that the opposite question—how a woman's height affects the number of children she has—has not been asked until now.

Daniel Nettle, of the Open University in Britain, has done so. And the answer, soon to be published in the *Proceedings of the Royal Society*, is that women do better reproductively if they are shorter than average. On the face of it, that is surprising. Given that tall men have more children, and that height is, at least in part, inherited, it might be expected that men would prefer tall women because they would produce tall (and so sexually successful) sons. But that is not the case. A woman's height is not a consideration in the eyes of most men.

However, an analysis of the lives of 5,000 women born in Britain in March 1958 suggests that short women have larger families than tall ones, an effect that is independent of such factors as the tendency of people from poor families to be shorter than those from rich ones. Dr Nettle suggests it is because short women become fertile earlier (the same hormonal processes that terminate growth are also responsible for sexual maturation). This increased number of children would counterbalance the sexiness of the sons of tall women, resulting in equal numbers of grandchildren and explaining why height *per se* is irrelevant to a woman's attractiveness to men. Tough on short men, though.

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Petroleum geology

The argument needs oiling

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At odds over the origins of oil

MILLIONS of years ago, tiny animals and plants died. They settled at the bottom of the oceans. Over time, they were crushed beneath layers of sediment that built up above them and eventually turned into rock. The organic matter, now trapped hundreds of metres below the surface, started to change. Under the action of gentle heat and pressure, and in the absence of air, the biological debris turned into oil and gas. Or so the story goes.

In 1951, however, a group of Soviet scientists led by Nikolai Kudryavtsev claimed that this theory of oil production was fiction. They suggested that hydrocarbons, the principal molecular constituents of oil, are generated deep within the earth from inorganic materials. Few people outside Russia listened. But one who did was J. F. Kenney, an American who today works for the Russian Academy of Sciences and is also chief executive of Gas Resources Corporation in Houston, Texas. He says it is nonsense to believe that oil derives from “squashed fish and putrefied cabbages”. This is a brave claim to make when the overwhelming majority of petroleum geologists subscribe to the biological theory of origin. But Dr Kenney has evidence to support his argument.

In this week's *Proceedings of the National Academy of Sciences*, he claims to establish that it is energetically impossible for alkanes, one of the main types of hydrocarbon molecule in crude oil, to evolve from biological precursors at the depths where reservoirs have typically been found and plundered. He has developed a mathematical model incorporating quantum mechanics, statistics and thermodynamics which predicts the behaviour of a hydrocarbon system. The complex mixture of straight-chain and branched alkane molecules found in crude oil could, according to his calculations, have come into existence only at extremely high temperatures and pressures—far higher than those found in the earth's crust, where the orthodox theory claims they are formed.

To back up this idea, he has shown that a cocktail of alkanes (methane, hexane, octane and so on) similar to that in natural oil is produced when a mixture of calcium carbonate, water and iron oxide is heated to 1,500°C and crushed with the weight of 50,000 atmospheres. This experiment reproduces the conditions in the earth's upper mantle, 100km below the surface, and so suggests that oil could be produced there from completely inorganic sources.

The opposition will take some convincing. Although crude oil is composed mostly of hydrocarbons, it does contain molecules such as porphyrins and sterols that are usually thought of as the product of biology. That has always been taken as evidence for oil's fossil origin. Dr Kenney counters that these molecules occur inorganically (they are found, for example, in certain sorts of meteorite). They might also be the products of bacteria that feed on oil.

A stronger criticism of his hypothesis—stronger because it is made on the grounds of thermodynamic stability on which he has chosen to fight—is that, even if his non-biological crude oil did form deep in the earth, its molecules would disintegrate as they rose towards the cooler, less pressured conditions of the surface. To examine the products of his experiments, Dr Kenney had to cool them suddenly; otherwise they would have disappeared. It is difficult to see how such cooling could happen in nature unless oil erupted rapidly from the mantle to the surface. On the other hand, if his thermodynamic calculations are correct, it is also difficult to see how crude oil could have arisen from squashed fish and putrefied cabbages.

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Terrorism in Italy

The life in death of Aldo Moro

Aug 15th 2002
From The Economist print edition

Italy's years of terror in the 1970s remain a subject for books, and even opera

IN ITALY, almost nothing seems straightforward. In a country where public life is ruled even more than elsewhere by ideology, corruption, back-scratching and hidden interests, the basic who-what-when-and-where of fact-driven reporting is all too easily swamped by the beguiling question of why. Looking for motives, usually secret, is a quest of such endless fascination that the Italian press even has a name for it: *dietrologia* or behind-the-scenes-ology, the study of what you can't see.

No event in modern Italy has provided as much material for conspiratorialists as the kidnap and murder in 1978 of the leader of the Christian Democrats, Aldo Moro, by the Red Brigades, a far-left terrorist group. Among its many repercussions, big and small, terrorism seized the attention of Leonardo Sciascia, a celebrated Sicilian author and politician who had already written extensively about that other threat to the authority of the Italian state, the mafia. The short book he wrote after the Moro affair quickly became, for some, a dietrological handbook. An extended edition of Sacha Rabinovitch's translation has just been published by Granta Books.

Moro was kidnapped one spring morning as he left the building where he lived on the Via Forte Trionfale in Rome. All five of his bodyguards were killed in the attack. He was held (probably in the city), put up for trial by a so-called people's court and then shot in the head. Fifty-four days after he was kidnapped, Moro's body was found, following a tip-off, in the back of a Renault 4 that had been parked, without difficulty, in the crowded heart of the city.

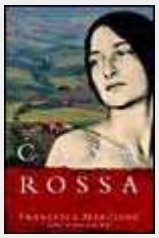
Moro's captors allowed him to write to his political colleagues and to read what they were saying about him in the newspapers. He begged them to consider negotiating with the terrorists, who offered to return him alive in exchange for the release of 13 fellow extremists on trial in Turin. Opinion was divided. Most Christian Democrats, as well as the Communist Party, were against bargaining with terror. Moro's colleagues who favoured this line believed he was writing

The Moro Affair
By Leonardo Sciascia; translated by Sacha Rabinovitch

Granta Books; 176 pages; £7.99

Buy it at
Amazon.co.uk

Casa Rossa
By Francesca Marciano



Pantheon; 352 pages; $25. Jonathan Cape; £12.99

Buy it at
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under duress or that he had lost his reason. When he realised that their view had prevailed, his letters turned to despair and rage.

Amazon.co.uk

These anguished letters encouraged countless conspiracy theories. Why would Christian Democrats abandon one of their own? For more than 30 years, they had monopolised power and blocked reform. Yet change was now inevitable. Moro, with his gloomy eyes and air of unfathomably patient *ennui*, was a master of obfuscation. As Sciascia observes, the principle of changing everything to change nothing, which Lampedusa's prince-hero espouses in “The Leopard”, could have applied perfectly to Moro. Yet, whatever his ultimate goal, by 1978, he had broken the shell of Christian Democratic politics and made a pact with the left, the *compromesso storico*, drawing the Communists into the arena of national government as responsible partners for the first time.

Find the motive

Many people in Italy, and some in Washington, feared and disliked this idea, and—although Italian politics has moved on—the belief has never entirely died that Moro was sacrificed on the altar of cold-war politics, perhaps even with a nod from America. In 1986, Giuseppe Ferrara made a film, “L'Affare Moro”, starring Gian Maria Volonte, which presented Moro as the victim of a power struggle among Christian Democrats. Sciascia was too sophisticated to make so crude a conspiratorial assumption, but his book remains grimly fascinating for the combination of intrigue and incompetence it lays bare.

It is difficult to remember quite how terrified Italians were in the 1970s—the *anni di piombo* or years of lead. That Moro was kidnapped by a disciplined unit in a country where organisation and efficiency were unknown must have meant that the Red Brigades had official sanction and foreign help. So many believed. That he could be kidnapped by a small band of nihilists who were more lucky than disciplined and killed because the Italian police were too inept and ill-led to find him was hard for many to swallow, even though that was more or less what the judges in all the five trials following the murder concluded.

Sciascia's book will soon be 25 years old. But Moro's murder and homegrown terrorism in general continue to trouble the Italian imagination. The broad canvas of Francesca Marciano's new novel, “Casa Rossa”, which Longanesi will publish in Italy next spring, stretches from fascism to the Red Brigades. It opens in the south—in Moro's native Puglia as it happens—where Alina, the heroine, is packing up the red-walled family house, sorting through three generations of violence and domestic betrayal: her grandmother's, her father's and, most of all, that of her sister, Isabella, who is in thrall to her lover, a terrorist. He and his friends shelter in the family house, but when, after a tip-off, they are tried and jailed, Alina too receives a sentence of sorts: any romantic or professional life is put on hold by the draining routine of weekly visits to her sister in prison.

As in her earlier book, “Rules of the Wild”, Ms Marciano casts a sharp eye on the society that surrounds the family of the Casa Rossa. Her Italy is full of lies. The big ones stop the nation from facing the world; the small have the advantage of helping the world go round. But the search for truth takes courage, and the lesson learned in her novel is that the violence of the *anni di piombo* achieved nothing.

Giving the victim voice

The emotional intensity of opera offers yet another approach to Italy's years of lead. “Non Guardate al Domani”, a competition entry by Filippo del Corno, who composed the music, and Angelo Miotta, a journalist who did the libretto, treats Moro's capture and death virtually as a passion play.

Employing Moro's letters to his party colleagues and to his wife as the spine of the work, it focuses less on behind-the-scenes intrigue than on the transformation of Moro himself in the wilderness of captivity, as he is obliged to confront his approaching end and examine his soul. At the same time, we hear in counterpoint the grey, obfuscating language of politics that Moro and his fellows use amongst themselves. This work, which it is hoped will be staged in Italy next year, takes the Moro affair out of the world of conspiracy into the realm of religious myth.

The Moro Affair.
By Leonardo Sciascia; translated by Sacha Rabinovitch.
Granta Books; 176 pages; £7.99

Casa Rossa.
By Francesca Marciano.
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Jonathan Cape; £12.99

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The British and their past

In love with decline

Aug 15th 2002
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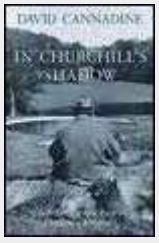
Is nostalgia a national failing, or are some Brits more prone than others?

ALAN COREN, a British humorist, was once advised that anyone seeking to catch the attention of the book-buying public should write about cats, golf or Nazis. In response he published a collection of essays entitled “Golfing for Cats”, with a picture on the front cover of a moggy in Nazi uniform wielding a putter. Perhaps it is similar thinking which has inspired David Cannadine, the director of London University's Institute for Historical Research, to call a collection of his historical essays “In Churchill's Shadow”. Churchilliana sells well in both Britain and the United States.

In Churchill's Shadow: Confronting the Past in Modern Britain
By David Cannadine



Allen Lane, The Penguin Press; 386 pages; £25.

Buy it at Amazon.co.uk

In reality just two and a bit of the 12 essays in Mr Cannadine's volume are directly concerned with Churchill. The rest range entertainingly over a variety of topics from the operettas of Gilbert and Sullivan to the James Bond novels to the diplomatic dabbling of a great Cambridge historian, G.M. Trevelyan. In a preface, Mr Cannadine argues that all of these essays, written over a period of some 20 years, are connected by Britain's sense of “vanishing supremacies and diminishing possibilities, the feeling that things were no longer as great or as stable or as splendid as they once had been”. Even if most of the essays are not actually about Churchill, Mr Cannadine suggests that he remains the dominant figure in this book if only because his career spanned the entire transition from late-Victorian imperialism to the end of empire after the second world war.

Britain's adjustment to its diminishing power and to the loss of empire is a recurring theme in Mr Cannadine's essays. It is this that provides the sometimes thin connecting thread between the various topics in the book. For unlike many celebrators of Churchill, Mr Cannadine is less interested in victory and heroic defiance than in Britain's reactions to its declining power. He suggests that Churchill “died a sad and disappointed man: for during his lifetime and despite his heroic efforts to prevent it, Britain ceased to be a great power”. In different ways most of these essays fit into the general theme of what have become known as decline studies.

The essay on Ian Fleming, the creator of James Bond, is as much a piece of literary criticism as historical research, although none the worse for that. Mr Cannadine shows how the Bond stories looked both backwards and forwards, venerating the toughness, patriotism and austerity of the Victorian era, while also revelling in the flashy materialism and sexual freedom of a more louche era. A delightful article on Noel Coward chronicles that playwright and entertainer's transition from anti-establishment gadfly in the 1920s—the man who said you should try everything once except incest and morris-dancing—to super-patriot in the second world war and embittered self-exile in Jamaica, lamenting the decline of moral standards and the loss of British colonies.

Perhaps the best article in the book is one of the two devoted wholly to Churchill. Mr Cannadine describes how the great man developed his speech-making skills, but also reminds us that in the years running up to the second world war Churchillian rhetoric was often treated as dated and over-blown. His contemporary Herbert Samuel said in 1935 that “the House of Commons always crowds in to hear him. It listens and admires but it remains unconvinced, and in the end it votes against him.” So much the worse for the lesser mortals surrounding Churchill, is how most people would react nowadays. But Mr Cannadine makes the further point that many of Churchill's fiery speeches were wasted on unworthy subjects—the futile fight to keep India part of the empire, for example. As a result, “his closely argued and powerfully documented speeches against the Nazi threat attracted much less notice than they deserved”.

The implication of this collection of essays, subtitled “Confronting the Past in Modern Britain”, is that the people and topics Mr Cannadine chooses to write about are somehow typical of the national dilemma. Yet that is questionable. Noel Coward and Winston Churchill may have had a shared horror at the loss of empire. But it is far from clear that the British as a whole shared their views. Indeed as Mr Cannadine notes at one point: “The British Empire may have been won in a ‘fit of absence of mind', but as far as the majority of the population seems to have been concerned, it was given away in a fit of collective indifference.” Yet that conclusion suggests that Mr Cannadine's latest addition to the field of decline studies, while unfailingly interesting, may say less about modern Britain than it claims.

In Churchill's Shadow: Confronting the Past in Modern Britain.
By David Cannadine.
Allen Lane, The Penguin Press; 386 pages; £25.
(To be published in the United States by Oxford University Press in spring 2003)

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British popular fiction

From Holmes to Harry Potter

Aug 15th 2002
From The Economist print edition

BESTSELLERS are in the air at the moment. A recent BBC television series "Reading the Decades" took a ten-yearly census of the books that had got people reading, talking and, most importantly, buying, during the post-war period. Now Clive Bloom extends that enquiry back to the beginning of the 20th century, by when Britain could be said to have become unequivocally literate (at the outbreak of the first world war only 1% of the population was still unable to read).

The reasons behind this sudden need to investigate what kinds of books people want to buy (or borrow, for Mr Bloom pays special attention to the role of local libraries in keeping sales of authors such as Catherine Cookson and Frederick Forsyth in their millions) are not hard to guess. The recent staggering commercial success of "Harry Potter", the proliferation of "chick lit" and "lad lit", and the upsurge of interest in the kind of history books that used to get given to resentful teenagers by worthy godparents, have all made publishers and critics re-think their assumptions. Mr Bloom makes the point that until the late 1980s British publishing houses were remarkably hit-and-miss in their market research: books were still commissioned largely on the basis of hunches and personal contacts. But readers are a wilful bunch who have ideas of their own about how they want to fill their shrinking leisure time and it makes sound sense to discover exactly which titles have historically made them part with their cash.

Bestsellers: Popular Fiction Since 1900
By Clive Bloom

Palgrave Macmillan; 312 pages; $60 and £45 (hardback); £14.99 (paperback)

Buy it at
Amazon.com
Amazon.co.uk

Mr Bloom, who is an academic, is aware that tables of statistics do not make for easy reading. In any case, he points out that it is nearly impossible to get your hands on reliable figures. Even now there is no such thing as a definitive bestseller list, simply a series of approximate guesses compiled by various national newspapers and bookselling chains. So instead Mr Bloom does that sensible thing of seeking out the telling anecdote or surprising example, the one which illustrates a larger point. Thus he emphasises that it was the paperback publication of "Lady Chatterley's Lover" in 1960 that caused all the fuss. As long as D.H. Lawrence's novel was available only in hardback, and so accessible to a well-heeled and supposedly educated market, no one turned a hair. It was the fact that paperbacks were associated with a mass market readership ("the wife and servants" of the trial judge's summing up) which made them such a potentially subversive force.

The second half of "Bestsellers" consists of potted biographies of popular authors from 1900 until the present day. Here you will recognise familiar friends like Conan Doyle, Dennis Wheatley and Ruth Rendell, and reacquaint yourself with Ethel M. Dell, Mary Renault and Grace Metalious (women, says Mr Bloom, dominate popular fiction as both writers and readers). Because it falls so clearly into two distinct halves, "Bestsellers" does not quite have the compelling drive associated with the best kind of popular writing. But as an informed and witty companion to what people read and why, it is excellent.

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By Clive Bloom.
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Destroying books in Russia

Hardly worth the trouble

Aug 15th 2002 | MOSCOW
From The Economist print edition

The perils of semi-historical fiction

RUSSIAN literary wars have grown tamer with the years. Not so long ago writers risked exile, labour camp or even death for books that did not suit the powers that be, whether Tsarist or Soviet. These days, the worst punishment they face is a short prison term, probably suspended, and harassment by self-styled patriotic youths. Still, it is a mischief even bad writers do not deserve.

Shocking as it sounds, Vladimir Sorokin, a plump, middle-aged Russian post-modernist, could soon be in prison for one of his books. He is a literary target of a pro-Kremlin youth movement called Moving Together, which is run by people with connections to the president's office. Earlier this year, they destroyed copies of Mr Sorokin's books (among others) outside the Bolshoi Theatre in Moscow, which they were picketing for having commissioned a script from him. Moving Together has since lodged a criminal complaint against Mr Sorokin with the Moscow prosecutor's office.

The offending book is a novel called “Goloboye Salo” (Blue Lard), which swarms with naughty words and, more provocatively, with the sexual couplings of famous or infamous modern Russians. In one passage of some length and descriptive detail, we are invited to picture the rut of a cloned Soviet dictator, Joseph Stalin, with a clone of his successor, Nikita Khrushchev.

In the past few days, Mr Sorokin has attended the first hearing in the trial on the criminal charges of disseminating pornography. If found guilty, he could face two years in prison. But the case looks weak and the fact that the prosecutors in charge asked Mr Sorokin for an autograph does not bode well for his angry young critics.

If he escapes jail, Mr Sorokin may yet find a silver lining to this sorry affair. Since the bringing of the charges, the sales of his rather mediocre works are said to have risen more than fivefold. His publishers may even print an eighth run of “Blue Lard”, an unheard-of feat for contemporary Russian fiction. Nor will his status as a literary martyr harm his chances in the approaching race for the Russian Booker prize, the country's most prestigious literary award, for which he has recently been shortlisted.

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New music

Uncontrolling the controllable

Aug 15th 2002
From The Economist print edition

Modernist technique meets fascination with nature in a neglected composer

HIS enormous output of operas, symphonies, concertos and chamber music must make Per Norgard one of the most prolific composers of our time. Yet though well known in his native Denmark, where he lives, the star-hungry music industry has not yet caught him in its spotlight, and his restless, probing music is woefully under-represented on the international scene. In Britain at least this neglect has been corrected with an appearance this summer at the Cheltenham festival and a performance at the London proms of his sixth symphony under Thomas Dausgaard, conducting the Danish National Symphony orchestra, which premiered it in Copenhagen two years ago. You could not hear a better introduction to his music: it is one of the most dynamic, impulsive works of recent years.

The symphony's descriptive subtitle, “At the End of the Day”, might suggest millennial prophecy or a nostalgic summing-up of his own career (he was 70 this year). But Mr Norgard's sixth is typically too complex and ambiguous to be stuffed into tight programmatic categories. One day leads to the next, he quietly notes, and the piece is, if anything, about renewal. The first of three movements, or passages as Mr Norgard calls them, opens with the glittering sounds of violins and piccolos, before dropping suddenly towards the growling depths of contrabass trombone and contrabass tuba. These two dramatic opening minutes close with an uneasy drumroll, and at that moment it seems as if the music has reached an unexpected and premature end.

But out of a tiny timpani figure, the work springs into life again, and this kind of musical rejuvenation repeats itself, with “little, unseen things”, as Mr Norgard puts it, providing the basis for a subsequent section. The whole piece continues in this state of flux, ceaselessly transforming itself from one soundworld to the next, from one emotional extreme to another. The music has an almost natural pulse without ever sounding repetitive. Change is its only constant.

The idea of continuous development has always held special fascination for Mr Norgard, both as it relates to his own position within the classical tradition, and in compositional terms. He sees his work as part of a Scandinavian symphonic tradition. The teacher who had the greatest influence on him was Vagn Holmboe, one of Denmark's best known and most prolific symphonists, with whom Mr Norgard studied in Copenhagen during the early 1950s. A more distant, but still powerful influence is Sibelius. Mr Norgard wrote to the great Finn in 1954, near the end of his life and long after he had ceased to compose, to say how modern he had always found his music.

Ordered chaos

Technically Mr Norgard's music, particularly the works of the late 1960s and the 1970s, was marked by exploitation of his so-called infinity series. The maths is complicated, but the result is easy enough to grasp: an indefinitely extendable row of notes that unfolds according to the simplest of rules in nevertheless unpredictable shapes. The patterned variety that emerges can be seen as the musical equivalent of a mathematical fractal.

The composer employed the infinity row in its purest form in a 1968 orchestral piece, “Voyage into the Golden Screen”. In this work—the title was taken from a pop song by Donovan—versions of the series are played at different speeds simultaneously, creating a multi-layered, hierarchical music. This is not the only experiment Mr Norgard plays with musical time. He also composes pieces that seem to accelerate continuously.

Many of Mr Norgard's recent pieces are based on microtones, pitches that are found in the cracks

between the 12 western semitones. A new violin concerto, “Borderlines”, which premiered at Cheltenham, hovers on the brink between different tuning systems.

Yet for all their complexity, Mr Norgard always aims to make his compositional systems serve an expressive purpose. Unlike some of his modernist contemporaries, for whom formal clarity is all, Mr Norgard is not afraid of dramatic features such as building and releasing tension. “I've been looking for music,” he says, “where when you hear something, you also hear something else at the same time. That ambiguity is a very human thing.”

To return to his sixth symphony, listening to it makes for a strongly emotional experience. It is almost like witnessing a force of nature: with its persistent bass tones and sudden climaxes, a small earthquake perhaps or a tsunami. Almost, but not entirely. You can also appreciate the music's elemental force and generative power on its own account.

Don't forget the composer

Though the likeness is tempting, Mr Norgard is wary about running too far with music-nature metaphors. Composing, he points out, involves more than searching out natural patterns. It is also a process of healing: “As a composer, you have a special wound, a special scar,” he says. “As an artist, you are never healed.”

The coda of his sixth symphony offers a good example of what he is talking about: the music seems to return to the shimmering soundworld of the opening, but weird, percussive rumblings break in once more on this serene surface. Underground sounds of this kind are the seeds of Mr Norgard's newest orchestral work, “Terrains Vagues” (2001). In his eighth decade, he continues to believe in compositional renewal, saying with quiet humour, “I still feel I'm at the beginning of something.”

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About sponsorship

Tran Do

Aug 15th 2002
From The Economist print edition

Tran Do, a dissident in Vietnam, died on August 9th, aged 78

Corbis

ONE afternoon in June last year Tran Do visited a shop in Ho Chi Minh City that had a copying machine. He took from his briefcase an 83-page manuscript. He wanted 15 copies, please. The shopkeeper said it would take some time. Mr Do said he would wait; at the age of 77 he had acquired the virtue of patience. Eventually the 15 copies were carried to Mr Do's car. Shortly after he drove away he was stopped by security police and ordered to drive to a nearby police station. There the 15 copies were removed and Mr Do was asked about their content. He said they contained his thoughts about life in Vietnam. He was told that he could go, for now, but the manuscript and the copies would be retained for examination. Mr Do never got them back.

No one other than officials has seen them, and it likely that they have been destroyed. However, it is a reasonable guess that they repeated some of Mr Do's criticisms of the government, among the sharpest made by a Vietnamese; that it should be reformed, drawing on the experience of western democracy. Such talk was all the more galling for Vietnam's leaders because they had thought of Tran Do as a person like themselves. He had fought against the French, the colonial power, and then against the United States, rising to the rank of general. After Vietnam's independence in 1976 he had been rewarded with a top job, as head of the Communist Party's culture department.

In 1998 this seeming stalwart wrote a letter to the party Politburo, with copies to “concerned citizens”, proposing that the party should give up its monopoly of power. The letter found its way to the outside world through the Internet. Mr Do was expelled from the party he had belonged to for 58 years. A search of his home produced diaries showing that he had been thinking for years that life in Vietnam had become “less and less like what we dreamed of building”. His letter to the party was not a sudden whim. For the party leaders that is what made it particularly alarming.

The unacceptable

Tran Do could have been jailed. In March this year the American State Department estimated that Vietnam held 150 political prisoners. Among the “prisoners of conscience” known to Amnesty International are a number whose views were similar to those of Mr Do. But, awkwardly for the authorities, Mr Do was a much decorated war hero who had fought alongside Ho Chi Minh. It would be difficult to dismiss him as a traitor. Nor could his actions be attributed to senility. His letter was carefully argued. More worryingly, he had friends. When Mr Do was expelled, a number of military veterans resigned from the party in protest. Did others in authority secretly sympathise with his views?

In his letter Mr Do said state-run projects were poorly managed and open to corruption. Party bosses in rural areas were getting rich at the expense of farmers. The Politburo might have accepted this as valid criticism. There have been similar grumbles in party newspapers. Less acceptable was Mr Do's contention that a market economy could not flourish under Soviet-style controls, and that Marxist-Leninism, though valuable in Vietnam's revolutionary days, was now outmoded. Mr Do then attacked “the party's absolute control of everything”, with just a few people taking key decisions. He did not specifically demand a multi-party system and free elections, but he came close to doing so, calling for “a true democracy”. Not everything in the West was “reactionary, decadent and deceitful”, he wrote. Other countries had rights “that we have never implemented and don't know how to”. Vietnam as a French colony was run better than it was now.

Members of the Politburo were hurt as much as angered by the letter. They believed that they were gradually making Vietnam a better place. Their citizens had “guided” freedom; and like their Communist neighbour China, Vietnam had an “open door” to foreign investment. But Mr Do was a reminder that they remain authoritarian states however many Big Macs are consumed.

The Politburo decided that Mr Do should not be detained but would be watched. Police would call on his wife and children, and encourage them to remind Mr Do of his duties to the nation. If he behaved himself, the letter incident would be allowed to fade from memory; eventually he might even be readmitted to the party. But having started a battle, the former general saw no alternative but to see it through. Mr Do wrote other “open” letters, and published a number of pamphlets. He asked permission from the authorities to start an independent newspaper. It was refused, but at the time of his death he was planning to go ahead with it anyway.

With his experience of government, he knew where security was weak, particularly in Ho Chi Minh City, previously Saigon, the capital of defeated South Vietnam. Being caught there was probably the result of over-confidence. Soon after, Mr Do became ill and he died in hospital. Nature has officially brought the Tran Do problem to a conclusion. What remains is the contention of a thoughtful old warrior that unless the regime changes it will collapse. Will it be heeded? Probably not.

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Overview

Aug 15th 2002
From The Economist print edition

America's Federal Reserve left its key interest rate unchanged at 1.75%, but said that the balance of risks is now tilted toward “economic weakness”, rather than inflationary strength. Labour productivity continues to grow, with non-farm output per hour increasing by 1.1% at an annual rate in the second quarter. But that was far slower than the 8.6% growth of the previous quarter. Retail sales in June grew by 1.2%, a better than expected rise. Much of this growth, however, was due to cheap financing schemes for cars; excluding automobiles, retail sales were weak. Wholesale prices fell by 1.1% in the year to July, after falling by 2.1% in the year to June.

Inflation in the **euro area** remains tame. In **France**, consumer prices rose by 1.6% in the year to July, up from 1.4% in the year to June. Annual consumer-price inflation in **Spain** remained unchanged in July at 3.4%; in **the Netherlands** it increased to 3.5% in July from 3.4% in June.

The ZEW index of **German** economic confidence plunged by 25.7 points to 43.4 in August. Any reading above zero indicates that most respondents expect the economy to improve. Analysts had expected the index to fall by only two points. The decline in confidence has raised new fears that the economic recovery is stalling. Germany's 12-month trade surplus ballooned to $100.6 billion in June, compared with $62.4 billion a year earlier. Germany's $22.2 billion current-account deficit in the year to June 2001 has reversed dramatically, becoming a 12-month surplus of $27.2 billion this June.

In June, **Japan's** current-account surplus was 90% up on a year earlier, thanks to strong exports and the effect of the World Cup. Although the **yen** is getting stronger, appreciating by 2.8% over the week on a trade-weighted basis, this has yet to have any discernible effect on the trade balance, which chalked up an $80.6 billion surplus over the last 12 months.

Annual consumer-price inflation in **Britain** increased to 1.5% in July from 1.0% in June. Excluding mortgage interest payments, inflation rose to 2.0%, still below the Bank of England's 2.5% target. Britain's goods deficit widened sharply to £3.0 billion in June, the largest deficit since December 2001. Imports fell by £960m, but exports fell by a full £2.2 billion, reversing last month's export surge.

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Output, demand and jobs

Aug 15th 2002
From The Economist print edition

% change on year ago

	GDP 1 qtr*	GDP 1 year	The Economist poll GDP forecasts 2002	2003	Industrial production latest	Retail sales (volume) latest	Unemployment % rate latest	year ago
Australia	+ 3.6	+ 4.2 Q1	+ 4.0	+ 3.8	+ 4.3 Q1	+ 6.3 Q2	6.2 Jul	6.9
Austria	+ 0.3	– 0.6 Q1	+ 0.9	+ 2.6	+ 1.6 May	– 1.1 Apr	4.1 Jun	3.5
Belgium	+ 1.8	– 0.3 Q1	+ 1.3	+ 2.9	– 2.5 May	– 3.3 May	11.8 Jul†	11.1
Britain	+ 3.8	+ 1.5 Q2	+ 1.7	+ 2.9	– 6.6 Jun	+ 4.6 Jun	5.1 Jun‡	5.0
Canada	+ 6.0	+ 2.1 Q1	+ 3.3	+ 3.5	+ 0.5 May	+ 4.3 May	7.6 Jul	7.0
Denmark	+ 1.4	+ 1.1 Q1	+ 1.6	+ 2.4	+ 4.2 Jun	+ 1.5 Apr	5.1 Jun	5.2
France	+ 1.4	+ 0.3 Q1	+ 1.4	+ 2.7	nil Jun	– 2.5 Jun	9.0 Jun††	8.6
Germany	+ 0.7	– 1.2 Q1	+ 0.7	+ 2.3	– 2.3 Jun	– 5.2 Jun	9.9 Jul§	9.3
Italy	+ 0.9	+ 0.2 Q2	+ 1.0	+ 2.5	– 5.4 Jun	– 0.2 May	9.0 Apr	9.5
Japan	+ 5.7	– 1.6 Q1	– 0.3	+ 1.1	– 2.9 Jun	– 3.5 Jun	5.4 Jun	4.9
Netherlands	+ 0.4	+ 0.3 Q1	+ 1.0	+ 2.5	– 3.0 Jun	– 2.1 May	2.5 Jun**	2.0
Spain	+ 2.1	+ 2.0 Q1	+ 2.1	+ 3.0	– 4.4 Jun	na	11.5 Jun	10.6
Sweden	+ 2.4	+ 2.1 Q2	+ 1.7	+ 2.9	+ 1.9 May	+ 4.9 May	4.0 Jun†	4.4
Switzerland	+ 0.7	+ 0.2 Q1	+ 1.0	+ 2.3	– 8.8 Q1	– 3.0 Jun	2.6 Jul†	1.7
United States	+ 1.1	+ 2.1 Q2	+ 2.7	+ 3.4	+ 0.2 Jun	+ 5.4 Jun	5.9 Jul	4.6
Euro area	+ 1.3	+ 0.3 Q1	+ 1.1	+ 2.6	– 1.2 May	+ 0.7 May	8.4 Jun	8.0
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*							
Finland	– 0.6	– 2.0 Q1	na	na	+ 5.5 Jun	+ 2.4 Apr	9.0 Jun†	9.3
Greece	na	+ 4.3 Q1	na	na	+ 2.4 Jun	+ 9.9 Apr	na	na
Iceland	na	+ 3.12001	na	na	+ 3.3 2001	na	2.3 Jun†	1.2
Ireland	na	+ 2.9 Q1	na	na	+16.0 Jun	+ 0.3 May	4.3 Jul	3.7
Luxembourg	na	+ 3.52001	na	na	+ 4.3 May	+ 4.9 Mar‡‡	2.7 May	2.4
New Zealand	+ 4.3	+ 4.0 Q1	na	na	+ 4.3 Q1	+ 8.3 Q2	5.1 Q2	5.3
Norway	– 1.1	+ 1.0 Q1	na	na	+ 5.3 Jun	+ 2.9 Jun	3.8 Q2	3.6
Portugal	+ 1.4	+ 1.4 Q1	na	na	– 0.7 Jun	– 1.5 Jun	4.5 Q2†	3.9

*% change at an annual rate. †Not seasonally adjusted. ‡April-June; claimant count rate 3.1% in July. §EU harmonised rate 8.3%. **Apr-Jun. ††Revised series. ‡‡New series.

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Prices and wages

Aug 15th 2002
From The Economist print edition

% change on year ago

	Consumer prices			The Economist poll consumer prices forecast		Producer prices			Wages/earnings		
	latest		year ago	2002	2003	latest		year ago	latest		year ago
Australia	+ 2.8	Q2	+ 6.0	+ 2.8	+ 2.6	– 1.1	Q2	+ 5.6	+ 4.3	Q1	+ 5.6
Austria	+ 1.7	Jun	+ 2.8	+ 1.7	+ 1.7	– 1.0	Jul	+ 1.9	+ 2.4	Jun	+ 2.7
Belgium	+ 1.3	Jul	+ 2.7	+ 1.7	+ 1.6	+ 2.4	Jun	+ 0.9	+ 2.6	Q2	+ 2.6
Britain	+ 1.5	Jul	+ 1.6	+ 1.9	+ 2.4	+ 0.3	Jul	– 0.1	+ 3.9	Jun	+ 4.7
Canada	+ 1.3	Jun	+ 3.3	+ 1.7	+ 2.2	– 1.2	Jun	+ 1.5	+ 2.8	May	+ 0.7
Denmark	+ 2.2	Jul	+ 2.4	+ 2.3	+ 2.0	– 0.9	Jul	+ 2.7	+ 4.0	Q1	+ 3.8
France	+ 1.6	Jul	+ 2.1	+ 1.8	+ 1.4	– 1.5	Jun	+ 2.3	+ 3.9	Q1	+ 4.3
Germany	+ 1.0	Jul	+ 2.6	+ 1.4	+ 1.2	– 0.8	Jul	+ 2.2	+ 2.1	Apr	+ 1.5
Italy	+ 2.2	Jul	+ 2.9	+ 2.3	+ 1.9	– 0.8	Jun	+ 2.4	+ 2.4	Jun	+ 2.7
Japan	– 0.7	Jun	– 0.8	– 1.0	– 0.5	– 2.2	Jul	+ 0.7	– 3.2	Jun	+ 2.1
Netherlands	+ 3.5	Jul	+ 4.6	+ 3.6	+ 2.3	– 2.2	Jun	+ 4.3	+ 3.0	Jun	+ 5.1
Spain	+ 3.4	Jul	+ 3.9	+ 3.3	+ 2.7	+ 0.5	Jun	+ 2.4	+ 4.0	Q1	+ 3.4
Sweden	+ 2.0	Jun	+ 2.9	+ 2.4	+ 2.1	– 0.6	Jun	+ 2.2	+ 4.1	May	+ 3.6
Switzerland	– 0.1	Jul	+ 1.4	+ 1.0	+ 1.2	– 1.6	Jul	+ 0.2	+ 2.5	2001	+ 1.3
United States	+ 1.1	Jun	+ 3.2	+ 1.6	+ 2.2	– 1.1	Jul	+ 1.4	+ 3.2	Jul	+ 4.1
Euro area	+ 1.9	Jul	+ 2.8	+ 2.1	+ 1.6	– 1.1	Jun	+ 3.2	+ 3.3	Q1	+ 2.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 1.8	Jul	+ 2.6	na	na	– 1.9	Jun	+ 1.9	+ 3.2	Q1	+ 5.1
Greece	+ 3.3	Jul	+ 3.9	na	na	– 0.1	Jun	+ 5.4	na		na
Iceland	+ 3.2	Aug	+ 7.9	na	na	+ 6.2	Jul	+ 6.7	+ 6.9	Jun	+ 8.2
Ireland	+ 4.2	Jul	+ 4.8	na	na	– 1.3	Jun	+ 5.0	+ 8.9	Q1	+ 7.4
Luxembourg	+ 2.0	Jul	+ 3.0	na	na	– 1.3	Jun	+ 0.1	+ 0.9	May	+ 2.7
New Zealand	+ 2.8	Q2	+ 3.2	na	na	+ 2.8	Q1	+ 8.0	+ 2.1	Q2	+ 1.8
Norway	+ 1.6	Jul	+ 2.7	na	na	– 9.4	Jul	– 3.2	+ 4.6	Q1	+ 4.4
Portugal	+ 3.4	Jul	+ 4.3	na	na	– 3.8	Jun	+ 4.2	– 0.2	Jun	– 0.6

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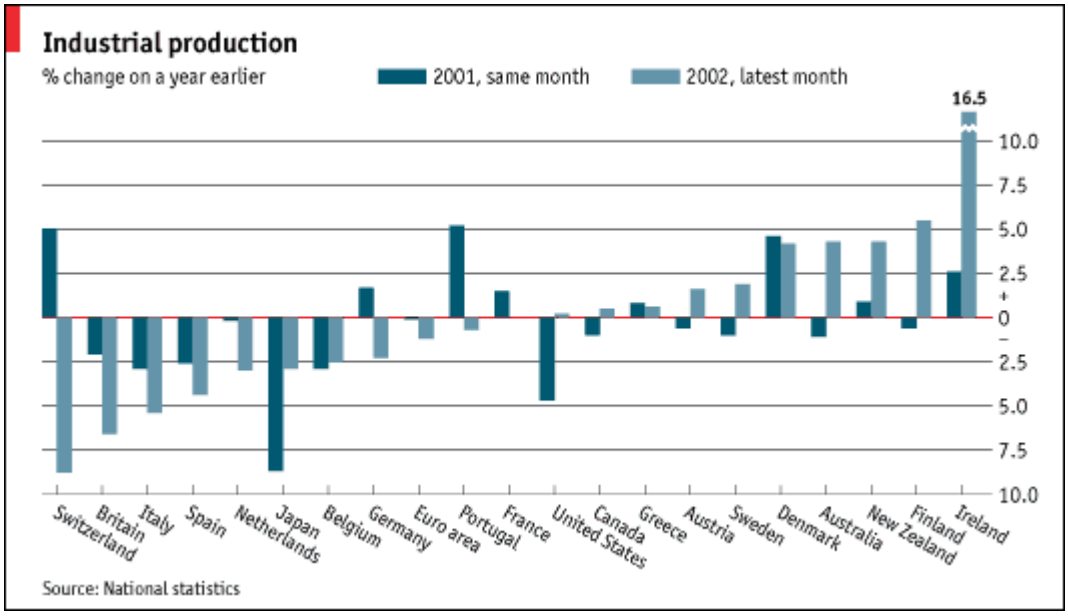
Industrial production

Aug 15th 2002
From The Economist print edition



In only four of the 20 countries in our chart has industrial production risen in each of the past two 12-month periods. In six countries, plus the euro area, it has fallen for two years on the trot. The sharpest swing in fortune has been in Switzerland, where output has fallen by 8.8% in the past year, partly thanks to the strong franc, after rising by 5.0% in the previous 12 months.

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Money and interest rates

Aug 15th 2002
From The Economist print edition

	Money supply* % change on year ago			Interest rates % p.a. (Aug 14th 2002)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	– 1.3	+12.3	Jun	4.93	5.01	4.81	5.52	5.78	6.55
Britain	+ 9.6	+ 6.5	Jun	3.91	4.91	3.85	4.53	4.91	5.73
Canada	+14.5	+ 5.8	Jun	2.78	3.97	3.24	5.10	5.58	7.10
Denmark	+ 3.2	+ 7.3	Jun	3.55	4.75	3.86	4.66	5.02	6.82
Japan	+30.6	+ 3.3	Jul	0.02	0.03	0.01	1.28	1.30	1.36
Sweden	+ 2.5	+ 7.3	Apr	4.17	4.25	4.38	4.91	5.02	4.90
Switzerland	+ 8.5	+ 4.3	Jun	0.81	3.15	1.12	2.80	3.22	4.06
United States	+ 5.7	+ 7.2	Jun	1.69	3.53	2.08	4.04	5.07	6.51
Euro area†	+ 6.9	+ 7.1	Jun	3.33	4.36	3.36	4.38	4.75	5.56

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 4.93%, Japan No.240 1.27%. Central bank rates: US fed funds 1.75%, ECB refinancing 3.25%, BOJ overnight call 0.002%, BOE repo 4.00%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholmsbörsen, UBS Warburg, DRI-WEFA, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Aug 15th 2002
From The Economist print edition

1995=100

	Aug 6th	Aug 13th*	% change on one month	% change on one year
Dollar index				
All items	72.0	73.4	– 0.3	+ 6.7
Food	75.6	77.7	+ 2.2	+10.7
Industrials				
All	67.3	67.6	– 3.9	+ 1.0
Nfa†	70.6	70.9	+ 0.3	+ 3.1
Metals	64.5	64.8	– 7.4	– 0.9
Sterling index				
All items	73.9	75.6	+ 2.3	– 1.1
Euro index				
All items	98.3	98.8	+ 3.1	– 2.1
Yen index				
All items	92.7	93.1	+ 2.6	+ 4.4
Gold				
$ per oz	305.70	314.95	– 1.0	+14.7
West Texas Intermediate				
$ per barrel	27.15	27.95	+ 0.7	– 0.5

* Provisional. † Non-food agriculturals.

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Stockmarkets

Aug 15th 2002
From The Economist print edition

Market indices

	Aug 14th	2002 high	2002 low	% change on one week	% change on record high	% change on Dec 31st 2001 in local currency	% change on Dec 31st 2001 in $ terms
Australia (All Ordinaries)	3,046.4	3,440.0	2,937.8	+ 1.6	-11.4	- 9.3	- 4.5
Austria (ATX)	1,131.8	1,357.2	1,114.4	+ 0.8	-34.8	- 0.7	+10.0
Belgium (Bel 20)	2,135.7	2,899.8	2,001.6	+ 0.8	-42.0	-23.2	-14.9
Britain (FTSE 100)	4,171.1	5,323.8	3,777.1	+ 1.9	-39.8	-20.1	-15.2
Canada (Toronto Composite)	6,550.1	7,958.1	6,161.1	+ 1.0	-42.5	-14.8	-12.9
Denmark (KBX)	179.1	233.4	169.0	- 0.6	-40.6	-20.3	-11.6
France (SBF 250)	2,184.8	3,081.9	2,067.7	- 0.9	-50.2	-26.7	-18.8
(CAC 40)	3,240.8	4,688.0	3,023.7	- 0.9	-53.2	-29.9	-22.3
Germany (Xetra DAX)	3,589.9	5,462.6	3,332.7	+ 3.6	-55.5	-30.4	-22.9
Italy (BCI)	1,155.5	1,513.0	1,077.8	+ 0.7	-47.1	-19.4	-10.6
Japan (Nikkei 225)	9,638.4	11,979.9	9,420.9	- 2.0	-75.2	- 8.6	+ 2.8
(Topix)	952.6	1,139.4	922.5	- 1.0	-67.0	- 7.7	+ 3.8
Netherlands (AEX)	347.2	531.2	318.5	+ 3.0	-50.5	-31.5	-24.1
Spain (Madrid SE)	636.8	848.1	625.9	+ 0.1	-44.4	-22.8	-14.4
Sweden (Affarsvarlden Gen)	150.3	236.8	143.5	+ 0.4	-62.5	-35.1	-27.3
Switzerland (Swiss Market)	5,266.8	6,694.1	4,607.8	+ 4.2	-37.4	-17.9	- 7.9
United States (DJIA)	8,743.3	10,635.3	7,702.3	+ 3.4	-25.4	-12.8	-12.8
(S&P 500)	919.6	1,172.5	797.7	+ 4.9	-39.8	-19.9	-19.9
(Nasdaq Comp)	1,334.3	2,059.4	1,206.0	+ 4.2	-73.6	-31.6	-31.6
Europe (FTSE Eurotop 300)*	929.8	1,279.7	862.3	+ 1.5	-45.5	-26.3	-18.3
Euro area (FTSE Ebloc 100)*	773.7	1,125.1	732.5	+ 1.1	-50.1	-30.4	-22.9
World (MSCI)†	829.6	1,024.4	756.7	+ 3.9	-42.7	na	-17.3
World bond market (Salomon)‡	499.8	499.8	430.3	+ 2.3	nil	na	+13.7

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms.
‡Salomon Smith Barney World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Aug 15th 2002
From The Economist print edition

	Trade balance*, $bn latest 12 months	Current account $bn latest 12 mths	Current account The Economist poll % of GDP, forecast 2002	Current account The Economist poll % of GDP, forecast 2003	Exchange rate trade-weighted† Aug 14th	Exchange rate trade-weighted† year ago	Currency units per $ Aug 14th	Currency units per $ year ago	Currency units per £	Currency units per euro	Currency units per ¥100	Budget balance % of GDP 2002‡
Australia	– 0.1 Jun	– 9.5 Q1	– 3.4	– 3.4	71.4	72.6	1.86	1.90	2.87	1.83	1.59	0.1
Austria	– 2.0 May	– 1.3 May	– 1.9	– 1.7	na	100.4	1.01	1.10	1.56	–	0.87	-0.3
Belgium	+ 15.1 Jun	+ 13.0 Dec	+ 4.8	+ 4.9	na	99.3	1.01	1.10	1.56	–	0.87	nil
Britain	– 45.6 Jun	– 31.2 Q1	– 2.0	– 1.9	105.0	104.2	0.65	0.70	–	0.64	0.56	-0.8
Canada	+ 34.7 May	+ 14.7 Q1	+ 2.4	+ 2.5	75.9	78.3	1.56	1.53	2.41	1.54	1.34	1.0
Denmark	+ 7.2 Jun	+ 3.5 Jun	+ 1.7	+ 1.7	103.2	102.6	7.53	8.17	11.6	7.43	6.46	2.2
France	+ 8.5 May	+ 26.2 May	+ 1.7	+ 1.6	na	102.0	1.01	1.10	1.56	–	0.87	-2.0
Germany	+100.6 Jun	+ 27.2 Jun	+ 1.2	+ 1.1	na	99.0	1.01	1.10	1.56	–	0.87	-2.8
Italy	+ 9.3 May	– 2.9 May	nil	nil	na	72.8	1.01	1.10	1.56	–	0.87	-1.4
Japan	+ 80.6 Jun	+107.0 Jun	+ 2.8	+ 2.8	138.8	139.6	117	120	180	115	–	-8.0
Netherlands	+ 23.7 Jun	+ 7.2 Q1	+ 4.0	+ 4.2	na	98.3	1.01	1.10	1.56	–	0.87	0.1
Spain	– 36.9 May	– 16.5 May	– 2.1	– 1.8	na	74.4	1.01	1.10	1.56	–	0.87	-0.3
Sweden	+ 14.3 Jun	+ 8.3 Jun	+ 3.3	+ 3.4	76.6	76.0	9.37	10.1	14.5	9.25	8.04	2.1
Switzerland	+ 2.7 Jun	+ 25.7 Q1	+ 9.8	+10.1	114.6	109.2	1.48	1.67	2.29	1.46	1.27	na
United States	–430.3 May	–398.1 Q1	– 4.4	– 4.7	112.4	116.9	–	–	1.54	0.99	0.86	-1.0
Euro area	+ 72.7 May	+ 20.2 May	+ 0.4	+ 0.5	81.7	79.6	1.01	1.10	1.56	–	0.87	-1.5
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 12.5 May	+ 8.6 Jun	na	na	na	78.5	1.01	1.10	1.56	–	0.87	3.2
Greece	– 18.8 Mar	– 6.7 Mar	na	na	na	57.6	1.01	1.10	1.56	–	0.87	0.4
Iceland	+ 0.1 Jun	– 0.2 Q1	na	na	na	na	85.9	98.3	133	84.8	73.7	-0.5
Ireland	+ 33.9 May	– 0.4 Q1	na	na	na	88.1	1.01	1.10	1.56	–	0.87	0.1
Luxembourg	– 2.9 May	+ 1.7 Q1	na	na	na	99.3	1.01	1.10	1.56	–	0.87	2.2
New Zealand	+ 0.2 Jun	– 1.2 Q1	na	na	83.9	81.3	2.16	2.31	3.34	2.13	1.85	0.1
Norway	+ 25.3 Jun	+ 26.1 May	na	na	104.3	94.8	7.55	8.90	11.7	7.45	6.48	14.0
Portugal	– 12.7 May	– 9.3 May	na	na	na	89.6	1.01	1.10	1.56	–	0.87	-2.4

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †1990=100, Bank of England. ‡OECD forecast.

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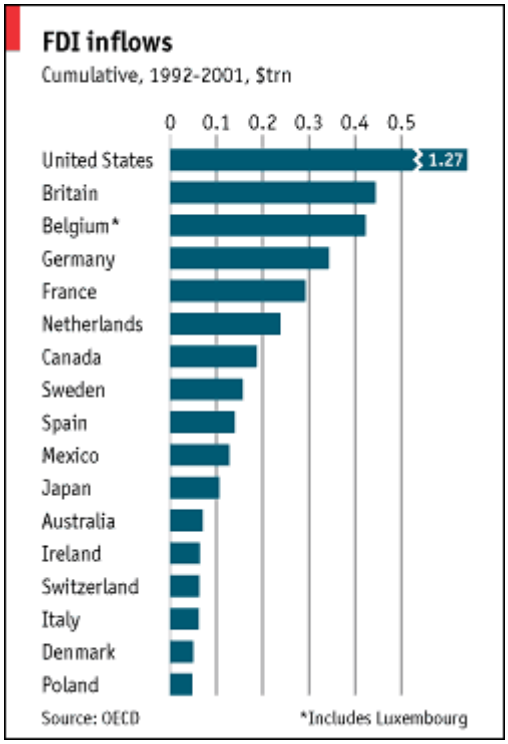
FDI inflows

Aug 15th 2002
From The Economist print edition



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Overview

Aug 15th 2002
From The Economist print edition

Industrial production is growing briskly in Asia, but is faltering in Latin America. **China's** industrial production grew by 12.8% in the 12 months to July, compared with 12.4% in the year to June; **India's** grew by 4.0% in the year to June, up from 3.8% in the year to May. In the year to June, **Brazil's** industrial production grew by a meagre 0.7%; **Mexico's** fell by 0.7%.

The flooding of the Vltava river temporarily shut the **Czech Republic's** statistics bureau in Prague, delaying the country's economic data releases for the coming days.

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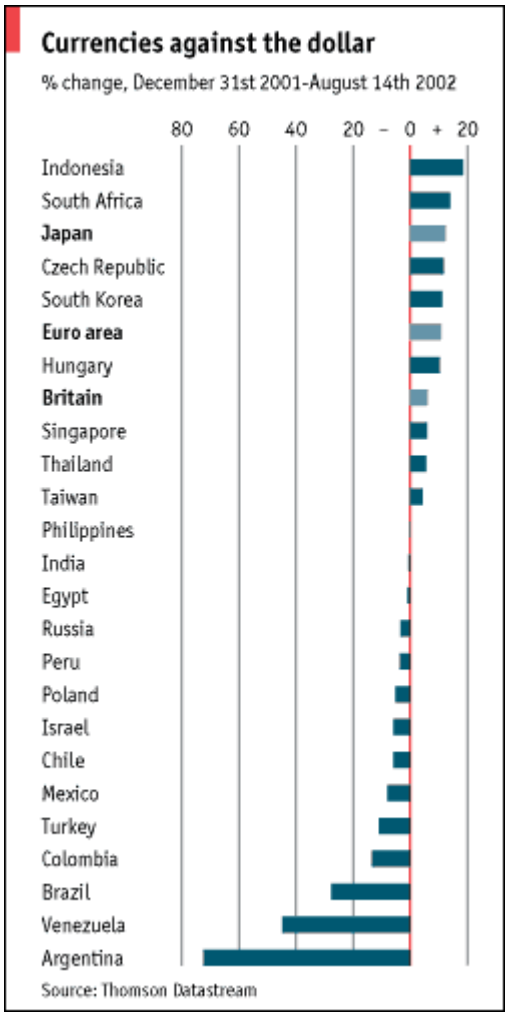
Currencies against the dollar

Aug 15th 2002
From The Economist print edition

So far this year, the yen and the euro have climbed by an eyebrow-raising 12% and 11% respectively against the dollar. Much more striking, however, have been the collapses of Latin American currencies: Argentina's peso has shed almost three-quarters of its value against the greenback; the Venezuelan bolivar has dropped by 45%; Brazil's *real* has fallen by 28%, with much of that decline during the past few weeks. The Indonesian rupiah and the South Korean won, both clobbered by the markets in 1998, have made strong gains this year. The South African rand, the Czech koruna and the Hungarian forint have also climbed by more than 10% against the dollar.



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Economy

Aug 15th 2002
From The Economist print edition

	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 8.0	Q2	+12.8	Jul	– 0.9	Jul	+28.3	Jul	+17.4	2001	241.9	May
Hong Kong	– 0.9	Q1	–11.6	Q1	– 3.3	Jun	– 8.5	Jun	+14.1	Q1	112.3	Jul
India	+ 6.4	Q1	+ 4.0	Jun	+ 4.2	Jun	– 5.4	Jun	+ 1.4	Q1	56.5	Jul
Indonesia	+ 3.5	Q2	– 9.4	Q4	+10.1	Jul	+27.5	Jun	+ 8.4	Q3	28.4	Jun
Malaysia	+ 1.1	Q1	+ 4.9	Jun	+ 2.1	Jul	+13.4	Jun	+ 7.0	Q1	32.4	Jun
Philippines	+ 3.8	Q1	+10.7	May	+ 2.6	Jul	+ 2.5	May	+ 5.6	Apr	13.5	Jul
Singapore	+ 3.9	Q2	+18.9	Jun	+ 0.1	Jun	+ 5.7	Jun	+17.5	Q2	80.3	Jul
South Korea	+ 5.7	Q1	+ 5.4	Jun	+ 2.1	Jul	+ 9.0	Jul	+ 5.7	Jun	112.4	Jun
Taiwan	+ 0.9	Q1	+ 8.4	Jun	+ 0.4	Jul	+18.6	Jul	+22.0	Q1	155.3	Jul
Thailand	+ 3.9	Q1	+ 6.2	Jun	+ 0.1	Jul	+ 3.8	Jun	+ 6.6	Jun	36.0	Jun
Argentina	–16.3	Q1	–12.4	Jun	+32.9	Jul	+12.6	Jun	nil	Q1	9.6	Jun
Brazil	– 0.7	Q1	+ 0.7	Jun	+ 7.5	Jul	+ 6.4	Jul	–18.1	Jun	41.9	Jun
Chile	+ 1.5	Q1	– 2.0	Jun	+ 2.6	Jul	+ 2.3	Jun	– 1.0	Q1	15.1	Jun
Colombia	+ 0.5	Q1	– 0.7	May	+ 6.2	Jul	+ 0.5	May	– 1.4	Q1	10.7	Jun
Mexico	– 2.0	Q1	– 0.7	Jun	+ 5.5	Jul	– 9.2	Jun	–16.8	Q1	45.5	Jun
Peru	+ 3.6	Jun	+ 2.8	May	nil	Jul	nil	May	– 1.0	Q1	8.7	Jun
Venezuela	– 4.2	Q1	–20.0	Mar	+22.0	Jul	+ 8.0	Q1	+ 1.8	Q1	6.7	May
Egypt	+ 4.9	2001†	+ 7.8	2001†	+ 2.8	May	– 8.4	Mar	– 0.1	Q1	12.7	Apr
Israel	– 4.2	Q1	+ 0.1	May	+ 6.6	Jun	– 6.4	Jun	– 2.3	Q1	22.8	Jul
South Africa	+ 2.1	Q1	– 0.1	Jun	+ 8.9	Jun	+ 3.5	Jun	– 0.1	Q1	5.9	Jun
Turkey	+ 2.3	Q1	+ 6.6	Jun	+41.3	Jul	– 9.7	May	– 2.0	May	22.3	Jun
Czech Republic	+ 2.5	Q1	+ 1.3	Jun	+ 0.6	Jul	– 2.5	Jun	– 2.4	Q1	21.4	Jul
Hungary	+ 2.9	Q1	+ 4.1	Jun	+ 4.6	Jul	– 2.3	Jun	– 1.9	Jun	10.2	Jun
Poland	+ 0.5	Q1	+ 2.2	Jun	+ 1.6	Jun	–10.6	Jun	– 6.6	Jun	27.1	Jul
Russia	+ 3.7	Q1	+ 4.4	Jun	+14.9	Jul	+42.4	Jun	+28.3	Q2	39.6	Jul
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Pakistan	+ 3.3	2001†	+21.3	Apr	+ 4.4	Jun	– 1.2	Jul	+ 0.3	2001†	4.1	May
Saudi Arabia	+ 1.2	2001	na		– 0.2	Apr	+44.1	2001	+14.5	2001	18.3	Jun

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Text refers only to the first 25 countries listed

Sources: National statistics offices, central banks and stock exchanges; Thomson Financial Datastream; Economist Intelligence Unit; Reuters; Warburg Dillon Read; J.P Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; *Russian Economic Trends*.

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Financial markets

Aug 15th 2002
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Aug 14th		Dec 31st 2001	
	Aug 14th	year ago	Aug 14th	% p.a.		one week	in local currency	in $ terms
China	8.28	8.28	12.8	na	1,718.4	– 1.3	+ 0.3	+ 0.3
Hong Kong	7.80	7.80	12.0	1.68	9,961.4	– 0.2	– 12.6	– 12.6
India	48.6	47.1	75.0	5.80	3,020.7	+ 0.4	– 7.4	– 8.1
Indonesia	8,775	8,775	13,554	15.24	447.7	+ 0.1	+ 14.2	+ 35.3
Malaysia	3.80	3.80	5.87	3.20	730.0	+ 1.2	+ 4.9	+ 4.9
Philippines	51.7	51.2	79.9	7.50	1,134.3	+ 4.0	– 2.9	– 3.2
Singapore	1.74	1.75	2.69	0.75	1,527.0	+ 2.2	– 5.9	– 0.4
South Korea	1,181	1,279	1,825	4.79	711.2	+ 4.7	+ 2.5	+ 14.0
Taiwan	33.5	34.6	51.8	2.00	4,887.4	+ 3.5	– 12.0	– 8.2
Thailand	41.9	44.9	64.7	2.00	371.2	+ 1.1	+ 22.2	+ 29.0
Argentina	3.63	1.00	5.60	66.00	368.9	+ 3.4	+ 24.9	– 65.6
Brazil	3.20	2.50	4.94	17.87	9,343.0	– 5.3	– 31.2	– 50.3
Chile	703	692	1,086	2.88	5,043.0	+ 0.8	– 6.6	– 12.1
Colombia	2,629	2,293	4,061	7.73	1,226.6	+ 3.0	+ 14.5	– 0.8
Mexico	9.97	9.10	15.4	6.70	6,053.6	+ 3.4	– 5.0	– 12.6
Peru	3.57	3.49	5.52	2.89	1,171.9	+ 1.3	– 0.3	– 3.8
Venezuela	1,376	729	2,125	30.24	6,948.9	– 1.9	+ 5.8	– 41.8
Egypt	4.62	4.25	7.14	7.18	5,301.0	+ 0.1	+ 0.5	– 0.5
Israel	4.69	4.24	7.24	6.40	350.2	– 1.6	– 21.6	– 26.2
South Africa	10.5	8.24	16.3	12.45	9,309.8	+ 0.8	– 10.8	+ 1.6
Turkey	1,635,000	1,475,000	2,525,421	42.00	10,038.5	– 4.6	– 27.2	– 35.2
Czech Republic	31.9	37.2	49.2	3.05	453.6§	+ 1.8	+ 15.0	+ 28.3
Hungary	249	276	385	9.65	7,091.6	+ 1.5	– 0.6	+ 9.6
Poland	4.17	4.26	6.44	8.55	12,910.5	+ 1.5	– 7.3	– 12.1
Russia	31.6	29.4	48.8	21.00	335.1‡	+ 2.8	+ 33.4	+ 28.9
EMF (MSCI)*	1.00	1.00	1.54	na	294.8	+ 2.5	na	– 7.1
EMBI+†	1.00	1.00	1.54	na	196.2	– 1.2	na	– 2.1

*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. § Aug 13th. ‡ In $ terms.

Sources: National statistics offices, central banks and stock exchanges; Thomson Financial Datastream; Economist Intelligence Unit; Reuters; Warburg Dillon Read; J.P Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; *Russian Economic Trends.*

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